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No. _____

OFFICE OF THE CLERK

IN THE
SUPREME COURT OF THE UNITED STATES

WILLIAM A. APPLING, et al.,
Petitioners,

v.

STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY, et al.,
Respondents.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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PETITION FOR WRIT OF CERTIORARI

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June 08, 2004

Counsel for Petitioner

QUESTIONS PRESENTED FOR REVIEW

1 May a federal court of appeals refuse to follow the doctrine of *stare decisis* on the ground that it would be "unfair" to a particular corporate litigant to do so?

2. Where a corporate litigant commits a fraud on the court (obtaining a judgment by falsely claiming to represent a material witness and fabricating positions for that witness), may a federal court of appeals refuse to set aside the judgment on the ground that there was no "miscarriage of justice" and the opposing party could have discovered the fraud?

LIST OF PARTIES TO THE PROCEEDINGS IN THE COURT BELOW

The petitioners (Plaintiffs/Appellants below) are:

William A. Appling, Joseph J. Kelly, Robert Buehler, John Lloyd, Daryl Mitchell, Richard Pyorre, John Weir, Gerard M. Verdi, William R. Sparks, Leonard D. Doctor, Jerry Lee Flanders, Verne Walton Ins., Larry K. Wilson, Michael C. Hartman, Daniel Brumfield, Martin H. Lefton, Douglas H. Perry, Mathew N. Pickett, Jr., Jo Ann Searcy, William R. Cornelison, Marilyn J. Cusimano, Dennis B. Farrell, Andrew W. Gaines, David B. Gordon, Paul Julian, Rosanne Smith, W.F. 'Bill' Burbank, Jr. Insurance Agency, Inc., Jean A. Cormier, Lee Cramer Insurance Agency, Inc., Franklin Dutto, Joan F. Ehler, Raymond C. Gilmore, Allen K. Golden, Richard O. Johnson, Gabriel O. Juarez, Jr., Bob Kennedy Insurance Agency, Inc., Lewis Insurance Agency, Inc., Lykke Insurance Agency, Inc., Robert C. Marshall, Terry L. Mcmanus, Alan L. Perkins, Dale W. Pitney, Jr., Jorge Sotelo Insurance Agency Inc., Anthony E. Vito, Terry D. Walker, Judy E. Weldin-leathers, Thomas A. Wilson, Michelle B. Pierce, aka Michelle B. Yates, Clifford K. Young, William Batchelder, Hooper Insurance Agency, Harold R. Little, Fred Love, Sam I. Mayeda, Jim Moore Insurance Agency, Inc., Michael L. Morgan, the Edward Pierce Insurance Agency, Inc., Dick Juge Insurance Agency, Inc., Paul Quilici, Bill Bernard Insurance Agency, Inc., Jacob Castroll, Reguera Insurance Agency, Inc., Chambers Insurance Agency Inc., Lee P. Saghirian, Tana P. Glockner, aka Tana P. Glockner-shultz, Kenneth E. Carroll; Richard S. Frank Insurance Agency, Inc., Bob Andras Insurance Agency, Inc., Patricia Adkins Insurance Agency, Inc., Joann M. Pergrem, aka Joann M. McWilliams,

The respondents (Defendants/Appellees below) are:

State Farm Mutual Automobile Insurance Company; State Farm Fire and Casualty Company; State Farm Life Insurance Company; State Farm General Insurance Company.

RULE 29 CORPORATE DISCLOSURE STATEMENT

With respect to the 16 petitioners who are incorporated, none has a parent corporation or a publicly held corporation owning any of its stock.

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PETITION FOR WRIT OF CERTIORARI

William A. Appling, et al ("Appling") respectfully petitions for a writ of certiorari to review the decision of a panel of the Ninth Circuit Court of Appeals.

OPINIONS AND ORDERS BELOW

The panel decision for which the writ of certiorari is requested is *William A. Appling, et al. v. State Farm Mutual Auto. Ins. Co., et al.*, 340 F.3d 769 (9th Cir. 2003), contained in the Appendix ("App") App. A at 1a through 33a. The Court of Appeals' decision denying the petition for rehearing is at App. B at 34a through 38a. The District Court decisions which the

panel reviewed are *William A. Appling, et al. v. State Farm Mut. Auto. Ins. Co., et al.*, Docket No. C-97-1569-MJJ (Northern District of California, January 7, 2000) and *William A. Appling, et al. v. State Farm Mut. Auto. Ins. Co., et al.*, Docket No. C-01-3181-MJJ (Northern District of California, February 4, 2002).

BASIS OF JURISDICTION

The panel decision and judgment for which review is sought was entered August 13, 2003.

An order denying the petition for rehearing was entered March 10, 2004.

28 U.S.C. § 1254 confers jurisdiction on this Court to review this decision by writ of certiorari.

COURT RULE INVOLVED

While the inter-circuit controversy over the citation and use of unpublished decisions continues to develop, the Ninth Circuit has adopted Circuit Rule 36-3(a), which provides as follows:

> Unpublished dispositions and orders of this Court are not binding precedent, except when relevant under the doctrine of law of the case, res judicata, and collateral estoppel.

Rule 36-3(a) was adopted for a 30-month period beginning July 1, 2000 and extended for an additional 30-month period beginning January 1, 2003.

STATEMENT OF THE CASE

The *Appling* plaintiffs filed this lawsuit against the State Farm group of insurance companies on April 29, 1997 in the federal district court for the Northern District of California. The basis for federal jurisdiction was 28 U.S.C. § 1332 (diversity of citizenship).

Each plaintiff was an insurance agent who had been operating under a contract to market and sell State Farm insurance products. The lawsuit included claims by many of the plaintiffs that State Farm had unilaterally terminated their contracts without good cause. State Farm maintained that it had the contractual power to terminate the contracts at will.

On May 13, 1999, while this lawsuit was pending in the district court, the Ninth Circuit Court of Appeals entered a nonpublished decision holding that the State Farm contract required good cause for termination. That decision, *Sandberg v. State Farm Mut. Auto. Ins. Co.*, 182 F.3d 927 (9th Cir. 1999) (mem. disposition), *cert. denied*, 528 U.S. 1118 (2000), is cited and discussed at length at various points in the decision for which this petition requests review on certiorari. (See App. A at 5a, 6a, 11a, 12a, 13a, 23a, 24a, 25a, 26a, and 27a.)

Ninth Circuit Rule 36-3(a) makes the *Sandberg* decision a binding precedent when relevant under the doctrine of collateral estoppel. (The rule is quoted on p. 2, *supra*.) Citing the rule and the *Sandberg* decision, the *Appling* plaintiffs whose contracts had been terminated moved in the district court for a

collateral-estoppel based summary judgment that the State Farm contract was at least reasonably susceptible to an interpretation that it could not be terminated without cause, which would allow their termination claims to go to the jury. State Farm cross-moved for a summary judgment that the contract was terminable at will, arguing that the district court should refuse to follow *Sandberg* because it would be "unfair" to State Farm. The district court denied the *Appling* plaintiffs' motion and granted State Farm's cross-motion.

The *Appling* plaintiffs appealed, contending that *Sandberg* was binding precedent in the Ninth Circuit under Circuit Rule 36-3, and the district court could not refuse to follow binding precedent.

While the appeal was pending, the *Appling* plaintiffs learned that, back during the discovery period leading up to the summary judgment phase in the district court, State Farm had fraudulently purported to represent a potential third-party witness, who held information highly material to the termination decision, and had advanced false positions on behalf of that person without his knowledge or consent. Upon learning this, the *Appling* plaintiffs filed an independent action to set aside the district court's decision granting State Farm's cross-motion on the termination issue, on the ground that the decision had been obtained by a fraud on the court. That action, was dismissed by the district court for failure to state a cause of action. The *Appling* plaintiffs appealed, and the two appeals were heard at the same time.

On August 13, 2003, the Ninth Circuit panel assigned to the two actions issued a 2-1 decision affirming the district court on both the collateral estoppel issue and the dismissal of the independent action. (The majority opinion is App. A at 1a-22a. The dissenting opinion is App. A at. 22a-33a.) With respect to the collateral estoppel issue, the majority concedes that the

Sandberg decision is relevant under the doctrine of collateral estoppel, overturning the district judge on that particular issue:

> [T]he district court erred by finding the termination-for-cause decision in *Sandberg* was not necessary to the holding. Contrary to the district court's conclusion, the prerequisite for applying collateral estoppel was met. *See Weems*, 49 F.3d at 532.

(App. A at 13a.) But the majority then refuses to follow Circuit Rule 36-3(a), which makes *Sandberg* a binding precedent when relevant under collateral estoppel. The majority concludes, instead, that it would be "unfair" to State Farm to follow *Sandberg*, essentially because, prior to the *Sandberg* decision, State Farm had managed to obtain earlier decisions over the years from other courts agreeing with its position that the contract was terminable at will. Apart from the legal error in refusing to follow its own precedent, the majority also errs in concluding that *Sandberg* was "contrary" to the earlier decisions.

With respect to the independent action to set aside the termination decision because of the fraud on the Court, the majority reasons that this was not a "miscarriage of justice" which "harms the integrity of the judicial process," characterizing State Farm's faked representation of the potential witness and fabrication of false positions for the witness as simple "non-disclosure" which could have been discovered by "due diligence." (App. A at 23a.)

The Dissent

The dissent concludes that the district court (and the majority) err as a matter of law in not applying collateral

estoppel against State Farm and in dismissing the independent action. With respect to the majority's decision not to follow *Sandberg*, the dissent states:

> The majority holds that collateral estoppel does not bar relitigation in this case of the identical issue that was decided in *Sandberg v. State Farm Mut. Auto. Ins. Co.*, 182 F.2d 927 (9th Cir. 1999) (memorandum disposition). *Sandberg* held that, under California law, the contract provisions that are at issue here permit termination only for good cause. The majority concedes that the district court erred in holding that the preconditions for estoppel were not met in this case, *see* majority opinion, *supra*, but the majority nonetheless defers to the district court's ultimate decision not to estop State Farm from relitigating the issue. The majority errs.

(App. A at 23a.)

> [T]he majority is wrong to defer to the district court's decision in disregarding *Sandberg*. The district court has no such discretion, and we owe the district court's decision on this point no deference. The district court held that our decision in *Sandberg* was sufficiently inconsistent with prior decisions *in other jurisdictions* (not our court) that it would be unfair to estop State Farm from relitigating the scope of the termination clauses at issue. In such circumstances, the lower court's refusal to follow a decision of this circuit is reversible error.

> The question of the consistency of *Sandberg* with prior decisions -- and, hence, in some sense *Sandberg*'s fairness -- was a matter for the panel that decided that case. It is improper to assume that the *Sandberg* panel was unaware of, or disregarded, the state of the law when it issued its disposition. Moreover, State Farm had amply opportunity to challenge the consistency (and fairness) of our decision with prior authority when it petitioned for rehearing by the original panel.

(App. A at 25a.)

> The district court has no special expertise nor license to assess, as a matter of law, whether our decisions are right, wrong, consistent, or inconsistent. That is, quite simply, our task (and that of the Supreme Court). Our decisions, whether memorandum dispositions or opinions, state the law of the circuit and must be followed by a district court in cases where they properly govern the issues presented. *See* Ninth Circuit Rule 36-3. The district court had no authority to disregard our decision.

(App. A at 26a.)

With respect to the majority's opinion that it would be "unfair" to State Farm to follow *Sandberg*, the dissent states:

> The majority's conclusion that *Sandberg* is "inconsistent" with other authority so as to preclude applying collateral estoppel against State Farm is simply wrong. To be inconsistent

in this sense, a decision must conflict with relevant legal authority on the same issue.

This case involves two groups of plaintiffs: (1) those from Arizona, California, Colorado, Iowa, Maryland, Nevada, Utah, and Washington -- states that the district court held follow a rule that permits extrinsic evidence to be used to illuminate the meaning of *unambiguous* contract terms; and (2) those plaintiffs from Florida, Idaho, Kansas, Louisiana, Nebraska, Ohio, and Texas -- states that the district court held permit the introduction of extrinsic evidence if a contract term in *ambiguous*. Neither party has challenged the district court's conclusions in this regard. Accordingly, the only authority that would be relevant in determining that *Sandberg* was "inconsistent" would need to be authority interpreting the rule of law that we applied in *Sandberg* -- that is, authority applying California law, or the law of a state that follows the same rule.

The pre-*Sandberg* authorities that State Farm proffers applied New Hampshire, law, Illinois law, New Mexico law, and Kansas law -- none of which is at issue here (except Kansas). Although State Farm cites three cases from California courts, two are from trial courts, and none of them is California Supreme Court authority. It is wrong to hold, on such a basis, that *Sandberg* is "inconsistent" with the law of California and of the other states that follow the same rule. Nor do any of the authorities that post-date our decision in *Sandberg* indicate that *Sandberg* is inconsistent.

***

> Nothing in *Parklane Hosiery* suggests that the Supreme Court intended to upset the usual channels of appellate review or to grant discretion to district courts to refuse to accord preclusive effect to prior judgments of their circuit courts. Nor does *Parklane Hosiery* suggest that we should defer to an inferior court within our jurisdiction as to the correct legal application of our own decisions. *Parklane Hosiery* involved the question of whether to grant preclusive effect to a decision by the Second Circuit in a case that was before a district court within the same circuit. *See Id.* at 324-25. But the Supreme Court did not reach the actual question presented here of whether a district court may disregard a prior decision by the court of appeals that sits above it on the ground that the circuit's decision conflicts with foreign authority. Although the Court noted that a general exception might be made for decisions that are inconsistent with prior decisions, it held that "none of the circumstances that might justify reluctance to allow the offensive use of collateral estoppel is present." *Id.* at 331.

(App. A at 24a-26a.)

With respect to the independent action to set aside the termination decision based on fraud on the court, the dissent states:

> The gravamen of the plaintiff's complaint in the independent action under Rule 60(b) is that State Farm's counsel, Orrick, Herrington &

Sutcliffe, committed fraud upon the court by responding to the plaintiffs' request to depose Henry Keller, a former State Farm executive, by fraudulently claiming to represent Keller and opposing the disposition on grounds that he was very elderly, had long been retired, and possessed no documents or knowledge concerning the subject matter of the lawsuit. In reliance on Orrick's representations, the plaintiffs claim, Orrick did not represent Keller and knew Keller possessed material evidence that strongly supported their claims and was willing and ready to testify.

The majority holds that Orrick's acts are not actionable because they do not rise to the level of fraud on the court or work a grave miscarriage of justice. I cannot agree. The majority's interpretation as to when a federal court may set aside a judgment is too narrow. Rule 60(b) permits a court, within a reasonable time, not more than one year after a judgment is entered, to grant a motion for relief from a judgment because of, inter alia, fraud on the court. *See* Fed. R. Civ. P. 60(b). After a year elapses, the rule also allows a party to bring an independent action to set aside a judgment for fraud on the court. The power to grant relief in an independent action is based in the court's inherent "power to vacate judgments on proof that a fraud on the court has been committed." *In re Levander*, 180 F.3d 1114, 1118 (9th Cir. 1999) (citing *Chambers v. NASCO, Inc.*, 501 U.S. 32, 43-44 (1991)). Rule 60(b) largely codified preexisting substantive law regarding the circumstances in which courts are

empowered to set aside judgments, but removed many procedural complexities that were associated with preexisting law. *See Averbach v. Rival Mfg. Co.*, 809 F.2d 101, 1020-21 (3rd Cir. 1987) (discussing the relationship of Rule 60(b) to prior law and practice). The period of a year specified by Rule 60(b) supplanted the earlier requirement that a request to set aside a judgment that was brought as part of the original action must have been made before end of the term of the court in which the judgment was entered. However, nothing in the text of Rule 60(b) requires that a plaintiff make a higher showing for relief in an independent action than in a motion under the rule.

The question presented here is whether the fraud that the plaintiffs have alleged may, if proved, warrant relief. Fraud in the discovery process plainly may sustain an independent action under Rule 60(b). The Supreme Court has held that federal courts may set aside judgments, notwithstanding the defense of laches or the plaintiff's lack of diligence in pursuing relief if a judgment has been obtained based on evidence that counsel has "manufactured." *See Hazel-Atlas Glass Co. v. Hartford-Empire Co.*, 322 U.S. 238 (1944). The Third Circuit has held that a plaintiff stated a claim for relief in an independent action based on opposing counsel's false and misleading answers to interrogatories. *See Averbach*, 809 F.2d at 1017, 1022-23. None of our precedents warrants a different result. In *Levander*, we stated that "non-disclosure by itself does not constitute fraud on the court" that warrants relief in an independent action under

> Rule 60(b), *Levander*, 180 F.3d at 1119, and that ordinary perjury similarly is not actionable, but we explicitly embraced a definition of fraud on the court that encompasses "fraud perpetrated by officers of the court so that the judicial machinery cannot perform in the usual manner its impartial task of adjudging cases." *Id.* at 1119 (quoting 7 James W. Moore, et., Moore's Federal Practice ¶ 60.33, at 515 (2nd Ed. 1978)).
>
> Here, Orrick is alleged not merely to have failed to disclose material evidence[1] that under long-established federal law it was obligated to disclose, but also to have claimed to represent a potential witness that it did not represent and intentionally to have misrepresented that person's position in a calculated attempt to obtain a judgment in its client's favor. An attorney in a legal proceeding who fraudulently claims to represent a client whom she or he does not, not only commits a fraud against the parties to the proceeding, but also a fraud on the court. Both the court and the parties are entitled to rely on an attorney's representation that she or he actually represents a client whom he or she claims to represent. A fraudulent misrepresentation about the fact, nature, and scope of an attorney's mandate is not only an ethical breach but a fraud of the highest order that interferes with the machinery of our judicial system. Our adversary system cannot function if attorneys claim to represent individuals that

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1 Keller himself advised Orrick that he had material evidence to furnish to the plaintiffs.

they do not. The majority fails to appreciate the gravity of Orrick's alleged fraud, and errs as a matter of law in holding that an allegation of such fraud may be dismissed for failure to state a claim.

The majority also errs by holding that the plaintiffs could have, with diligence, discovered Orrick's alleged duplicity by insisting on deposing Keller despite Orrick's representations and that the plaintiffs' failure to do so bars their claim. I strongly disagree. First, under *Hazel-Atlas*, the diligence of a party in discovering the alleged basis for setting aside a judgment is not decisive. *See Hazel-Atlas*, 322 U.S. at 246. Moreover, unlike the perjury in *Levander*, Orrick's alleged fraud will not be subject to the rigors of cross-examination in the factfinding process itself: The representation by counsel that he represents a witness and that the witness has no material information is not "testimony" that may be cross-examined. A party is entitled to rely on the representations of adverse counsel regarding such matters.

As a matter of construing the discovery rules, moreover, the principle that the majority embraces, namely that a party may not rely on the plain representations of adverse counsel in the discovery process, is not cynical but unworkable. It requires a party doggedly to pursue discovery notwithstanding opposing counsel's signed certification that such discovery is not warranted, *see* Fed. R. Civ. P. 26(g), on the possible chance that opposing counsel is committing fraud. The failure of the

party seeking discovery to take such action, which itself might violate the discovery rules, by the majority's lights, precludes it from seeking redress if it later discovers that it has been the victim of fraud. I cannot embrace such a view of the law.

Such an interpretation of the discovery rules is not only unconscionable, but flies in the face of the purpose of the rules themselves. As the Rules Advisory Committee has explained, Rule 26 explicitly imposes an affirmative duty "to engage in pretrial discovery in a responsible manner that is consistent with the spirit and purposes of Rules 26 through 37," Fed. R. Civ. P. 26, Advisory Committee Notes, 1983 Amendment, Subdivision (g), and Rule 37(c) permits a district court to sanction a party for making false or misleading discovery disclosures. *See* Fed. R. Civ. P. 37(c). As the Washington Supreme Court has held, the Federal Rules of Civil Procedure explicitly encourage the imposition of sanctions for discovery abuse in part because "a spirit of cooperation and forthrightness during the discovery process is necessary for the proper functioning of modern trials." *Wash. State Physicians Ins. Exch. & Ass'n v. Fissons Corp.*, 858 P.2d 1054, 1077 (Wash. 1993). The court noted that although "[f]air and reasoned resistance to discovery is not sanctionable[,] ... misleading ... responses [are] ... contrary to the purposes of discovery and ... most damaging to the fairness of the litigation process." *Id.* at 1079-80.

> The plaintiffs' allegations, if proved, would be most damaging to the ethical standing and professional reputation of any attorney -- and indeed might have severe collateral consequences such as disbarment.[2] The majority minimizes the gravity of the plaintiffs' charge and invites similar behavior in the future by holding that such a claim may be dismissed for failure to state a claim in an independent action under Rule 60(b). As Judge Schwarzer has persuasively explained: "Misconduct, once tolerated will breed more misconduct and those who might seek relief against abuse will instead resort to its self-defense." William W. Schwarzer, Sanctions Under the New Federal Rule 11 -- A Closer Look, 104 F.R.D. 181, 205. I would reverse the district court and reinstate the action.

(App. A at 28a-33a.)

REASONS FOR GRANTING THE WRIT

As the dissent explains, in detail, the *Sandberg* decision, a binding precedent under Ninth Circuit Rule 36-3(a), is *stare decisis* in this action. In the absence of a decision overruling

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2 The majority does not hold that Orrick and State Farm have not committed the actions as alleged, but merely that the plaintiffs may not seek relief under Rule 60(b). Orrick itself could be well-served by trial of the charges. They must be very disturbing to a reputable firm. If untrue, Orrick should welcome the opportunity to disprove them.

Sandberg from either the Supreme Court or an *en banc* panel of the Ninth Circuit, neither the district court nor a later panel has the discretion to refuse to follow *Sandberg*. *Stare decisis* is a bedrock principle of the judicial system. All circuits recognize and adhere to this fundamental principle, including the Ninth Circuit. See, e.g., *Hart v. Massanari*, 206 F.3d 1155, 1171 (9th Cir. 2001): "Circuit law ... binds all courts within a particular circuit, including the court of appeals itself."

Under Circuit Rule 36-3 the *Sandberg* decision, though unpublished, is "binding precedent" when relevant under the doctrine of collateral estoppel. The majority opinion concedes that *Sandberg* is relevant for purposes of collateral estoppel under *United States v. Weems*, stating that "the prerequisite for applying collateral estoppel was met." (App. A at 13a.)

At that point, as the dissenting opinion explains, "the district court had no discretion to refuse to follow our *Sandberg* decision" and "the majority is wrong to defer to the district court's decision in disregarding *Sandberg*." (App. A at 25a.) This was not an exercise of discretion by the district court. "[T]he lower court's refusal to follow a decision of this circuit is reversible error." (*Id.*)

The majority relies on *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 331 (1979) as support for the district court's decision to refuse to follow *Sandberg* (App. A at 13a) but, as the Dissent explains, "[n]othing in *Parklane Hosiery* suggests that the Supreme Court intended to upset the usual channels of appellate review or to grant discretion to district courts to refuse to accord preclusive effect to prior judgments of their circuit courts. Nor does *Parklane Hosiery* suggest that we should defer to an inferior court within our own jurisdiction as to the correct legal application of our own decisions." (App. A at. 26a.)

The majority's conclusion that it could depart from the *stare decisis* principle on the theory that it would be "unfair" to State Farm is not only a clear legal error (misapplying *Parklane Hosiery Co. v. Shore*, 439 U.S. 322 (1979), it is also based on an erroneous assumption that certain prior decisions were actually inconsistent with *Sandberg*.

In concluding that following *Sandberg* would be unfair to State Farm because *Sandberg* is supposedly inconsistent with other decisions, the majority erroneously refers to seven decisions which are *not* inconsistent with *Sandberg*. (*Olander, Peters, Mooney, Gardner, Drum, Melnick,* and *Vitkauskas*.) Each of those was decided under the older "plain meaning" or "textual" rule which *prohibits* the use of extrinsic evidence to interpret an integrated contract that appears to be unambiguous. *Sandberg* applied the very different California rule, a "contextual" rule that *requires* the court to examine the extrinsic evidence, even when the contract appears to be unambiguous. These two rules often produce different results. In the *Olander* case, for example, one of the supposed "inconsistent" decisions, the majority opinion distinguished *Sandberg* as follows:

> [I]n holding that summary judgment was inappropriate on the terminable-at-will issue, the court in *Sandberg* applied California law, which, unlike North Dakota law, permits the consideration of extrinsic evidence on the question of whether a contract is ambiguous.

Olander v. State Farm Mutual Automobile Insurance Co., 317 F.3d 807, 812 (8th Cir. 2003).

Noting that this case involves plaintiffs from several states which follow the "contextual" rule applied in *Sandberg*, the dissent explains that "the only authority that would be

relevant in determining that *Sandberg* was 'inconsistent' would need to be authority interpreting the rule of law that we applied in *Sandberg* -- that is, authority applying California law, or the law of a state that follows the same rule." (App. A at 24a.) "[T]he majority's conclusion that *Sandberg* is 'inconsistent' with other authority so as to preclude applying collateral estoppel against State Farm is simply wrong. To be inconsistent in this sense, a decision must conflict with relevant legal authority on the same issue." (*Id.*)

The majority also improperly assumes (apparently) that *Sandberg* disregarded five earlier decisions. (*Peters, Mooney, Melnick, Vitkauskas, and Scola.*) As the dissent explains, however:

> [T]he question of the consistency of *Sandberg* with prior decisions -- and hence, in some sense *Sandberg's* fairness -- was a matter for the panel that decided that case. It is improper to assume that the *Sandberg* panel was unaware of or disregarded the state of the law when it issued its disposition.

(App. A at 25a)

The majority's decision to affirm the dismissal of the independent action to set aside the judgment because of the fraud on the court is also a clear legal error.

The fraud which gave rise to the independent action is summarized by the dissent as follows:

> Orrick is alleged not merely to have failed to disclose material evidence that under long-established federal law it was obligated to disclose, but also to have claimed to represent a

> potential witness that it did not represent and intentionally to have misrepresented that person's position in a calculated attempt to obtain a judgment in its client's favor. An attorney in a legal proceeding who fraudulently claims to represent a client whom she or he does not, not only commits a fraud against the parties to the proceeding, but also a fraud on the court.
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> ***
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> Our adversary system cannot function if attorneys claim to represent individuals that they do not. The majority fails to appreciate the gravity of Orrick's alleged fraud, and errs as a matter of law in holding that an allegation of such fraud may be dismissed for failure to state a claim.

(App. A at pp. 30a-31a.) The dissent is correct. See, e.g., *Hazel-Atlas Glass Co. v. Hartford Empire Co.*, 322 U.S. 238, 246 (1944) (judgment vacated where litigant falsely attributed article prepared by litigant's attorney to a disinterested third party); *Pumphrey v. K.W. Thompson Tool Co.*, 62 F.3d 1128, 1133 (9th Cir. 1985) (independent action upheld where litigant failed to disclose unfavorable videotape).

The majority affirms a dismissal of this claim on the theory that these actions "did not disrupt the judicial process because the Agents through due diligence could have discovered the non-disclosure." (App. A at 22a.) This is a further legal error, which conflicts with the clear instruction of this Court in *Hazel-Atlas*:

> But even if Hazel did not exercise the highest degree of diligence Hartford's fraud cannot be

> condoned for that reason alone. ... [T]ampering with the administration of justice in the manner indisputably shown here involves far more than an injury to a single litigant. It is a wrong against the institutions set up to protect and safeguard the public, institutions in which fraud cannot complacently be tolerated consistently with the good order of society. Surely it cannot be that preservation of the integrity of the judicial process must always wait upon the diligence of litigants. The public welfare demands that the agencies of public justice be not so impotent that they must always be mute and helpless victims of deception and fraud.

Hazel-Atlas at 246. The Ninth Circuit follows *Hazel-Atlas* in this respect. See, e.g., *Pumphrey* at 1133.

CONCLUSION

The Court should allow a writ of certiorari to review the majority's decision, which departs from the fundamental principle of *stare decisis*, sanctions fraud on the court in a manner which damages the integrity of the judicial process, and conflicts directly with this Court's decision in *Hazel-Atlas Glass Co. v. Hartford Empire, Co.* 322 U.S. 238, 246 (1944).

DATED: June 08, 2004

Respectfully submitted:

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APPENDIX A

FOR PUBLICATION

United States Court of Appeals
FOR THE NINTH CIRCUIT

William A. Appling, Joseph J. Kelly, Robert Buehler, John Lloyd, Daryl Mitchell, Richard Pyorre, John Weir, Gerard M. Verdi, William R. Sparks, Leonard D. Doctor, Jerry Lee Flanders, Verne Walton Ins., Larry K. Wilson, Michael C. Hartman, Daniel Brumfield, Martin H. Lefton, Douglas H. Perry, Mathew N. Pickett, Jr., Jo Ann Searcy, William R. Cornelison, Marilyn J. Cusimano, Dennis B. Farrell, Andrew W. Gaines, David B. Gordon, Paul Julian Ins., Rosanne Smith, W.F. 'Bill' Burbank, Jr. Insurance Agency, Inc., Jean A. Cormier, Lee Cramer Insurance Agency, Inc., Franklin Dutto, Joan F. Ehler, Raymond C. Gilmore, Allen K. Golden, Richard O. Johnson, Gabriel O. Juarez, Jr., Bob Kennedy Insurance Agency, Inc., Lewis Insurance Agency, Inc., Lykke Insurance Agency, Inc., Robert G. Marshall, Terry L.	No. 00-16521 D.C. No. CV-97-01569-MJJ/ MEJ

McManus, Alan L. Perkins, Dale W. Pitney, Jr., Eleanor E. Rowland, Jorge Sotelo Insurance Agency Inc., Anthony E. Vito, Terry D. Walker, Judy E. Weldin-Leathers, Thomas A. Wilson, Michelle B. Pierce, aka Michelle B. Yates, Clifford K. Young, William Batchelder, Hooper Insurance Agency, Harold R. Little, Fred Love, Sam I. Mayeda, Jim Moore Insurance Agency, Inc., Michael L. Morgan, The Edward Pierce Insurance Agency, Inc., Dick Juge Insurance Agency, Inc., Paul Quilici, Bill Bernard Insurance Agency, Inc., Inc., Jacob Castroll, Reguera Insurance Agency, Inc., Chambers Insurance Agency, Inc., Lee P. Saghirian, Tana P. Glockner, aka Tana P. Glockner-Shultz, Kenneth E. Carroll; Richard S. Frank Insurance Agency, Inc., Bob Andras Insurance Agency, Inc., Patricia Adkins Insurance Agency, Inc., JoAnn M. Pergrem, aka JoAnn McWilliams,

Plaintiffs - Appellants,

V.

State Farm Mutual Automobile Insurance Company; State Farm Fire and Casualty Company; State Farm Life Insurance Company; State Farm General Insurance Company,

Defendants - Appellees.

William A. Appling; Leonard D. Doctor; Jerry Lee Flanders; Larry K. Wilson; Michael C. Hartman; Daniel Brumfield; Martin H. Lefton; Douglas H. Perry; Matthew N. Pickett, Jr.; Jo Ann Searcy; William R. Cornelison; Marilyn J. Cusimano; Dennis B. Farrell; Andrew W. Gaines; David B. Gordon; Rosanne Smith; Paul Julian Insurance Agency, Inc.; Verne Walton Insurance Agency, Inc.; Raymond C. Gilmore; Bob Kennedy Insurance Agency, Inc.; Lewis Insurance Agency, Inc.; Dale W. Pitney, Jr.; Anthony E. Vito; Terry D. Walker; Paul Quilici; Jacob Castroll,

Plaintiffs-Appellants,

v.

Orrick, Herrington & Sutcliffe;

No. 02-16452

D.C. No. CV-01-03181-MJJ

OPINION

State Farm Mutual Automobile)
Insurance Company; State Farm)
Fire and Casualty Company;)
State Farm Life Insurance)
Company; State Farm General)
Insurance Company,)
)
Defendants-Appellees.)

Appeal from the United States District Court
for the Northern District of California
Martin J. Jenkins, District Judge, Presiding

Argued and Submitted
March 31, 2003 -- San Francisco, California

Filed August 13, 2003

Before: Betty B. Fletcher, Alex Kozinski, and
Stephen S. Trott, Circuit Judges.

Opinion by Judge Trott;
Dissent by Judge B. Fletcher

COUNSEL

William P. Tedards, Jr., Washington, D.C., for the plaintiffs-appellants.

George A. Yuhas, Orrick, Herrington & Sutcliffe LLP, San Francisco, California, for the defendants-appellees.

Stephen A. Brick, Orrick, Herrington & Sutcliffe LLP, San Francisco, California, for the defendants-appellees.

OPINION

TROTT, Circuit Judge:

Plaintiffs-Appellants ("Agents") are independent-contractor insurance agents who sold insurance products for the State Farm group of insurance companies ("State Farm").[1] Each Agent has or had an independent-contractor agreement with State Farm ("contract").[2]

This consolidation appeal arises from an action the Agents brought in district court alleging that State Farm breached the contract ("breach of contract action"). The district court granted summary judgment in favor of State Farm on July 3, 2000. The Agents appeal this decision in Case No. 00-16521, arguing that the district court abused its discretion by not applying collateral estoppel against State Farm based on our unpublished decisions in *Sandberg v. State Farm Mut. Auto.*

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1 The State Farm group of insurance companies are (1) State Farm Mutual Automobile Insurance Company, (2) State Farm Fire and Casualty Company, (3) State Farm Life Insurance Company, and (4) State Farm General Insurance Company.

2 State Farm has modified the contract from time to time; however, each of the Agents had the AA660 (introduced in 1966), AA3 (introduced in 1977), or AA4 (introduced in 1982) version of the contract. Because the changes in the versions of the contract do not affect our analysis, we refer to all three versions as the "contract."

Ins. Co., 182 F.3d 927 (9th Cir. 1999) (mem. disposition), *cert. denied*, 528 U.S. 1118 (2000). The Agents also argue that a genuine issue of material facts exists as to: (1) whether the contract's termination provision required good cause before State Farm could terminate its agents; (2) whether State Farm breached the implied covenant of good faith and fair dealing by terminating some of the Agents; (3) whether the contract's provision granting State Farm the right to prescribe rules governing the binding, acceptance, renewal, rejection, or cancellation of risks allowed State Farm to implement a program that limited its risk exposure in certain geographic locations; and (4) whether State Farm breached the implied covenant of good faith and fair dealing by not giving the Agents permission to place rejected business with other insurance carriers. We have jurisdiction under 28 U.S.C. § 1291, and we affirm because we hold that there are no genuine issues of material fact on any of these claims.

On August 20, 2001, the Agents brought an independent action ("independent action") to set aside part of the summary judgment in their failed breach of contract action. In the independent action, Case No. 02-16452, the Agents alleged as a ground for relief that State Farm's counsel, Orrick, Herrington & Sutcliffe LLP ("Orrick"), committed fraud on the district court by (1) responding to a subpoena for information from a retired State Farm executive without the executive's permission, and (2) assuring the Agents' counsel that the retired executive did not have any documents or knowledge concerning the subject matter of the litigation. The district court dismissed the independent action pursuant to Federal Rule of Civil Procedure 12(b)(6) for failure to state a claim. We have jurisdiction under 28 U.S.C. § 1291, and we affirm because we hold that Orrick's actions do not amount to fraud on the district court.

BACKGROUND

A.

The Agents' breach of contract action arises from their contract with State Farm. The contract contained two integration clauses clearly superseding all prior agreements, and stating that changes to the terms of the contract could only be made by signed writings. The contract contained also the following provisions upon which the Agents based their claims.

1. "Termination Provision"

The Termination Provision states: "You or State Farm have the right to terminate this Agreement by written notice...." State Farm adopted this version of the provision in 1966. The prior version read: "This agreement may be terminated ... with or without cause, by either party or parties giving written notice to the other...." In 1966, State Farm also added a "Termination Review Provision" that did not appear in its prior version of the contract, providing for review of decisions made by State Farm to terminate the contract: "In the event we terminate this Agreement, you are entitled upon request to a review in accordance with the termination review procedures approved by the Boards of Directors of the Companies, as amended from time to time."

The Agents who brought the breach of contract action included some agents terminated by State Farm in March/April 1997.

2. "Risk Provision"

In response to catastrophic losses caused by Hurricane Andrew (1992) and the Northridge Earthquake in Southern California (1994), State Farm implemented programs to reduce

its risk exposure pursuant to the Risk Provision. The Risk Provision stated:

> We retain the right to prescribe all policy forms and provisions; premiums, fees, and charges for insurance; and rules governing the binding, acceptance, renewal, rejection, or cancellation [sic] of risks, and adjustment and payment of losses.

In September 1994, State Farm announced an exposure management program for the State Farm Fire and Casualty Company.[3] The program limited risk exposure growth that varied by geographic areas, called "exposure segments." These segments were determined by degrees of exposure to catastrophic loss. Those segments with the highest exposure were subject to the most stringent growth limitations -- a requirement that the agents not write new business until policyholders' non-renewal or relocation removed 4% of the existing business. Most segments, however, were not subject to growth limitations.

3. "Principal Occupation Provision"

State Farm refused to grant the Agents permission to place business rejected as a result of State Farm's program -- including the exposure management program -- with other insurance carriers. State Farm on the contract's Principal Occupation Provision, which stated:

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3 The Agents also challenged several other programs and procedures in the district court, which they do not mention in their opening brief. Any claims based on those programs and procedures are therefore abandoned on appeal. *Collins v. City of San Diego*, 841 F.2d 337, 339 (9th Cir. 1988).

> The fulfillment of this Agreement will be your principal occupation, and you will not directly or indirectly write or service insurance for any other company, other than a State Farm affiliate or through an assigned risk plan, or for any agent or broker, except in accordance with the terms of any written consent we may give you.[4]

B.

The basis for the Agents' independent action involved Orrick's response to an October 1998 subpoena issue in the breach of contract action and served on Henry Keller ("Keller"), a former State Farm executive who retired in 1976. The subpoena sought the following information:

> 1. Any and all documents regarding [State Farm] ... from, and including, January 1, 1988 to the present.
>
> 2. Any and all correspondence with any representative, employee, officer, director, agent, consultant or and all other persons working for or with [State Farm] ... from, and including, January 1, 1988 to present.

Keller contacted State Farm about the subpoena, and State Farm assured him they would handle the matter on his behalf. On November 9, 1998, Orrick responded to the subpoena on Keller's behalf by objecting to it. The Agents also allege that during a break at a deposition on November 19, 1998, Orrick

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4 State Farm revised this provision in 1977, but the difference between the two versions is not relevant to our analysis. We refer to both provisions as the "Principal Occupation Provision."

assured their counsel that Keller did not have any documents or knowledge concerning the subject matter of the litigation.

In January 2001, six months after the district court entered its summary judgment in the breach of contract action, the Agents discovered that Keller had not authorized State Farm to respond on his behalf, and was never shown a copy of the objections or consulted with respect to their contents. On August 20, 2001, the Agents brought the independent action to set aside the portion of the summary judgment in the breach of contract action relating to the Termination Provision. The Agents asserted that Orrick's actions regarding Keller were fraud on the court and that, without the fraud, Keller would have produced: (1) a 1997 letter Keller wrote to State Farm's President and CEO criticizing State Farm's handling of a new form contract; (2) a 1988 videotape interview of Keller, in which Keller states that the 1966 revision of the Termination Provision was in response to agent concerns about arbitrary terminations; and (3) a statement Keller made discussing the 1966 revision. The district court dismissed the independent action, holding that Orrick's actions regarding Keller were not fraud on the court.

DISCUSSION

I. Case No. 00-16521 -- The Agents' Appeal From the District Court's Summary Judgment in the Breach of Contract Action

We review a grant of summary judgment de novo. *Oliver v. Keller*, 289 F.3d 623, 626 (9th Cir. 2002). We must determine, viewing the evidence in the light most favorable to the nonmoving party, whether there are any genuine issues of material fact and whether the district court correctly applied the relevant substantive law. *Id.*

A.

The District Court Correctly Exercised Its Discretion By Refusing to Apply Collateral Estoppel

Generally, we review issues regarding collateral estoppel de novo. *United States v. 22 Santa Barbara Drive*, 264 F.3d 860, 868 (9th Cir. 2001). Offensive non-mutual collateral estoppel is a version of the doctrine that arises when a plaintiff seeks to estop a defendant from relitigating an issue which the defendant previously litigated and lost against another plaintiff. *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 329 (1979). District courts have discretion whether to apply offensive non-mutual collateral estoppel, and we may only reverse if they abuse that discretion. *Id.* at 331; *Resolution Trust Corp. v. Keating*, 186 F.3d 1110, 1114 (9th Cir. 1999); *Robi v. Five Platters, Inc.*, 838 F.2d 318, 330 (9th Cir. 1988). The Agents argued before the district court and on appeal that *Sandberg*, 182 F.3d 927, where we held that the Termination Provision required good cause before State Farm could terminate its agents, should apply to collaterally estop State Farm from relitigating here whether the Termination Provision required good cause.[5]

In *Sandberg*, State Farm terminated its independent-contractor agreement with Sandberg, one of its agents. 182 F.3d 927. Sandberg then brought a breach of contract claim against State Farm arguing that the same Termination Provision at issue in this case allowed State Farm to terminate for good cause only. *Id.* The district court disagreed and held that the Termination Provision allowed State Farm to terminate at-will.

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5 *Sandberg* is an unpublished disposition of this court that may not be cited to or by the courts of this circuit as precedent, but may be cited when relevant under the doctrine of collateral estoppel. 9th Cir. R. 36-3.

Id. On appeal, however, we held that the Termination Provision was reasonably susceptible to a termination-for-cause interpretation. *Id.* We noted that two extrinsic facts supported Sandberg's for-cause interpretation: (1) State Farm omitted the "with or without" language in its 1966 revision of the Termination Provision; and (2) in a 1977 article, State Farm's Vice President for Agencies discussed the company's termination review procedure and explained that termination would only occur when "the file clearly supports a serious violation of a contract agreement...." *Id.* Nevertheless, the district court refused to apply collateral estoppel against State Farm based on our decision in *Sandberg*. The district court concluded that to do so would be unfair to State Farm.

[1] Offensive non-mutual collateral estoppel applies where (1) the issue sought to be litigated is sufficiently similar to the issue presented in an earlier proceeding and sufficiently material in both actions to justify invoking the doctrine, (2) the issue was actually litigated in the first case, and (3) the issue was necessarily decided in the first case. *United States v. Weems*, 49 F.3d 528, 532 (9th Cir. 1995). State Farm does not dispute that the first two requirements are satisfied here, but argues that *Sandberg* did not necessarily decide that the Termination Provision required good cause. We disagree.

[2] *Sandberg* necessarily decided that the Termination Provision required good cause. The panel determined this predicate issue before holding that State Farm had good cause for termination. Otherwise the panel would have affirmed the district court's judgment that the agent's termination was appropriate under an at-will provision. *See, e.g., Id.* at 530-32 (holding that the government was collaterally estopped from trying to prove the defendant knew his property was used to grow marijuana because, in a previous case, the court found that the defendant was an innocent owner with no knowledge of the marijuana growing operation and refused to apply forfeiture on

one of two grounds asserted by the government). Moreover, the panel clearly thought that the decision was necessary to its holding because it examined State Farm's cause to terminate only after determining the Termination Provision required good cause. Thus, the district court erred by finding the termination-for-cause decision in *Sandberg* was not necessary to the holding. Contrary to the district court's conclusion, the prerequisite for applying collateral estoppel was met. *See Weems*, 49 F.3d at 532.

[3] But we affirm the district court's decision because, notwithstanding its erroneous conclusion on the "necessarily decided" question, it proceeded to balance the various fairness factors and held that the "stark landscape of inconsistent prior interpretations of the termination clause weighs heavily in favor of granting Sandberg no preclusive effect." The district court did not abuse its discretion by giving nearly conclusive weight to this factor. *See Parklane Hosiery*, 439 U.S. at 330-31 (holding that district courts have discretion to refuse to apply offensive non-mutual collateral estoppel against a defendant if such an application of the doctrine would be unfair). Allowing offensive non-mutual collateral estoppel may be unfair to a defendant "if the judgment relied upon as a basis for the estoppel is itself inconsistent with one or more previous judgments in favor of the defendant." *Id.* at 330; *see also Robi*, 838 F.2d at 330 (holding that the district court abused its discretion by applying collateral estoppel to preclude appellant from relitigating an issue where the judgment that generated issue preclusion was inconsistent with a judgment appellant obtained against the appellee, on whose behalf issue preclusion was asserted). The district court correctly noted that *Sandberg* is contrary to several other well-reasoned holdings in favor of State Farm that the same Termination Provision at issue here allowed State Farm to terminate the contract at-will. *See Olander v. State Farm Mut. Auto. Ins. Co.*, 317 F.3d 807, 812 (8th Cir. 2003) (en banc); *Peters v. State Farm*, No. 85-2177-S

(D. Kan. 1986) (holding that the same Termination Provision at issue here allowed State Farm to terminate at-will the independent-contractor agreement); *Mooney v. State Farm Ins. Cos.*, 344 F.Supp. 697, 699-700 (D.N.H. 1972) (same); *Ex parte Gardner*, 822 So.2d 1211, 1217-19 (Ala. 2001) (same); *Scola v. State Farm*, No. 1-46985 (Cal. Ct. App. 1981) (same); *Drum v. State Farm*, No. 991165 (Cal. Super. Ct. 1988), *aff'd* No. A087634 (2000) (same); *Lotten v. State Farm*, No. 97-01951 (Cal. Super. Ct. 1998) (same); *Melnick v. State Farm Mut. Auto. Ins. Co.*, 749 P.2d 1105, 1110-11 (N.M. 1988) (same); *see also Vitkauskas v. State Farm Mut. Auto. Ins. Co.*, 509 N.E.2d 1385, 1387-88 (Ill. App. Ct. 1987) (holding that the termination provision in a Building Plan Agreement between State Farm and the plaintiff-agent, which stated that "[e]ither party may terminate this Agreement by written notice," allowed termination at-will).

[4] In *Olander*, for example, Olander, a State Farm agent, was charged with murder after a violent altercation with a neighbor. 317 F.3d at 808. When Olander refused to take a leave of absence until the criminal charges were resolved, State Farm terminated his independent-contractor agreement. *Id.* at 808-09. Olander then brought a wrongful termination action against State Farm. *Id.* at 809. The Eight Circuit sitting en banc reversed a divided three-judge panel of that court, and held that the same Termination Provision at issue in this case allowed State Farm to terminate Olander at-will. *Id.* at 811-12. Because of the inconsistent judgments and therefore potential unfairness to State Farm, we hold that the district court correctly exercised its discretion here by refusing to apply offensive non-mutual collateral estoppel and deciding the issue on the merits.

B.

The Termination Provision Does Not Require Good Cause

[5] The Agents dispute the district court's conclusion that the Termination Provision allowed termination at-will, and argue that parol evidence can be used to interpret the provision to show that it required good cause. In *Pacific Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co.*, the California Supreme Court established rules governing use of parol evidence in determining the meaning of words in a contract where the contract otherwise is clear and unambiguous, and integrated. 442 P.2d 641, 644-46 (Cal. 1968) (en banc). A reviewing court must consider extrinsic evidence in determining whether the contractual language is "fairly susceptible" to the meaning urged by the movant. *Id.* at 646. If the court so decides, then the extrinsic evidence is admissible as relevant evidence to prove the meaning of the language. *Id.*

[6] *Pacific Gas*, however, makes clear that "extrinsic evidence is not admissible to add to, detract from, or vary the terms of a written contract," *Id.* at 645, but only to define the terms in the contract:

> [R]ational interpretation requires at least a preliminary consideration of all credible evidence offered to prove the intention of the parties. Such evidence includes testimony as to the circumstances surrounding the making of the agreement ... including the object, nature and subject matter of the writing ... so that the court can place itself in the same situation in which the parties found themselves at the time of contracting.

Id. at 645 (internal quotation marks, citations, and footnote omitted); *see also Masterson v. Sine*, 436 P.2d 561, 563 (Cal. 1968) (en banc) (stating the general rule that a party cannot use parol evidence to add to or vary the terms of an integrated contract). This rule "does no more than allow extrinsic evidence of the parties' understanding and intended meaning of the *Words used in their written agreement.*" *Brawthen v. H & R Block, Inc.*, 104 Cal.Rptr. 486, 490 (Cal. Ct. App. 1972) (emphasis added). If the court finds that the contract is not susceptible to alternative meanings, then it may proceed to determine the issue based on the plain meaning of the contract language.

The district court held that the plain meaning of the Termination Provision allowed termination at-will and that the evidence did not create a genuine issue of material fact on the issue of contract interpretation. The Agents argue that the Termination Provision is susceptible to a for-cause interpretation because: (1) State Farm deleted the "with or without cause" language in 1966 in response to agent concerns; (2) State Farm added the Termination Review Provision in 1966; (3) and State Farm commented in employee literature that State Farm would not terminate agents except in cases of serious infractions.

Here, the Agents are seeking to add a "good cause" term to the Termination Provision, not to interpret the words of that provision. The Termination Provision is clear and only requires written notice for termination, therefore State Farm's deletion of the "with or without cause" language does not create ambiguity. Moreover, State Farm's insertion of the Termination Review Provision does not compel a conclusion that the contract requires good cause for termination. *See, e.g., Olander*, 317 F.3d at 811 (holding that the Termination Review Provision did not make the Termination Provision ambiguous). On the contrary, the Termination Review Provision suggests

State Farm's desire to prevent arbitrary terminations without limiting its legal entitlement to terminate at-will by written notice. Finally, comments in employee literature and guidebooks about the agents' concern in 1966 do not indicate that the words "right to terminate this Agreement by written notice" required good cause.

[7] As an example of what it meant by use of extrinsic evidence to interpret the words in a contract, *Pacific Gas* pointed out that evidence of trade usage or custom has been admitted to show that the term "United Kingdom" in a motion picture distribution contract included Ireland. 442 P.2d at 645 n.6. Here, on the other hand, the Agents have not introduced any extrinsic evidence that interprets specific words in the Termination Provision; instead, the Agents have sought to introduce evidence grafting on a good cause requirement, a practice that *Pacific Gas* prohibits.

State Farm and the Agents point to competing California Court of Appeals decisions from different districts to support their respective arguments. State Farm relies on *Bionghi v. Metro. Water Dist.*, 83 Cal.Rptr.2d 388 (Cal. Ct. App. 1999). In *Bionghi*, the contract permitted termination by 30 days written notice. *Id.* at 391-92. Holding that the contract allowed termination at-will, the court noted that *Pacific Gas* merely allowed extrinsic evidence to interpret the words of the contract: "*Pacific Gas & Electric* is thus not a cloak under which a party can smuggle extrinsic evidence to add a term to an integrated contract, in defeat of the parol evidence rule." *Id.* at 393.

For their argument, the Agents rely on *Wallis v. Farmers Group, Inc.*, 269 Cal.Rptr. 299 (Cal. Ct. App. 1990). In *Wallis*, the agent's contract permitted termination by either party on three months notice. *Id.* at 305. The court found that because the clause was silent on the subject of good cause, it

was fairly susceptible to a meaning that there was an express oral agreement or an implied-in-fact agreement that the contract could be terminated only for cause. *Id.* at 306. To show an implied-in-fact agreement that Farmers could only discharge her for cause, the agent introduced affidavits of Farmer's officers stating they thought the termination provision required good cause. *Id.* at 306-07. *Bionghi* sharply criticized and refused to apply *Wallis*.

[8] We need not choose between *Bionghi* and *Wallis*. Federal courts sitting in diversity "are bound by the pronouncements of the state's highest court on applicable state law." *Ticknor v. Choice Hotels Int'l, Inc.*, 265 F.3d 931, 939 (9th Cir. 2001). *Pacific Gas* provides the necessary guidance to resolve this issue on appeal, and clearly prohibits the Agents' attempt to graft a good cause requirement onto the Termination Provision's plain language. Thus, the district court correctly held that there was no genuine issue of material fact as to the meaning of the Termination Provision.

C.

State Farm Did Not Breach the Implied Covenant of Good Faith and Fair Dealing by Terminating Some of the Agents

The Agents argue that even if State Farm had a right at-will to terminate the Agents, it employed that power in bad faith in violation of the implied covenant of good faith and fair dealing. California law implies the covenant of good faith and fair dealing in every contract to ensure one contracting party does not unfairly frustrate the other party's right to receive the benefits of their agreement. *Guz v. Bechtel Nat'l, Inc.*, 8 P.3d 1089, 1110 (Cal. 2000). The covenant "cannot impose substantive duties or limits on the contracting parties beyond those incorporated in the specific terms of their agreement." *Id.*

"Thus if the employer's termination decisions, however arbitrary, do not breach such a substantive contract provision, they are not precluded by the covenant." *Id.*; *see also Foley v. Interactive Data Corp.*, 765 P.2d 373, 400 n.39 (Cal. 1988) (en banc) ("[W]ith regard to an at-will employment relationship, breach of the implied covenant cannot logically be based on a claim that a discharge was made without good cause").

[9] The Agents cannot graft a good causes requirement onto the Termination Provision using the implied covenant of good faith and fair dealing where State Farm has terminated an at-will relationship according to an express contract provision. State Farm did not violate any substantive contract provision by terminating the Agents. Thus, the district court correctly granted State Farm summary judgment on this claim.

D.

The Risk Provision Allowed State Farm to Implement the Exposure Management Program

[10] The district court granted State Farm's summary judgment on the Agents' claim that the exposure management program was not authorized under the Risk Provision, which states "We [State Farm] retain the right to prescribe all policy forms and provisions; premiums, fees, and charges for insurance; and rules *governing the binding, acceptance, renewal, rejection, or cancellation [sic] of risks*, and adjustment and payment of losses." (Emphasis added). This provision is patently clear: State Farm has the right to prescribe rules governing risks. Because the exposure management program is a program governing risks, it is permissible under the Risk Provision. The fact that State Farm subsequently added language to clarify the Risk Provision does not suggest that the explicit language at issue did not authorize the exposure

management program. We hold that the district court properly granted summary judgment on this issue.

E.

State Farm Did Not Breach the Implied Covenant of Good Faith and Fair Dealing by Refusing the Agents Permission to Place Rejected Business with Other Carriers

As mentioned above, California law implies the covenant of good faith and fair dealing in every contract to ensure one contracting party does not unfairly frustrate the other party's right to receive the benefits of their agreement. *Guz*, 8 P.3d at 1110. "The covenant of good faith finds particular application in situations where one party is invested with a discretionary power affecting the rights of another. Such power must be exercised in good faith." *Carma Developers (Cal.), Inc., v. Marathon Dev. Cal. Inc.*, 826 P.2d 710, 726-30 (Cal.1992) (en banc) (holding that a clause in a commercial lease allowing the lessor to terminate the lease and recapture the allowing the lessor to terminate the lease and recapture the leasehold upon notice by the lessee of intent to sublet or assign had to be exercised in good faith).

[11] The covenant applies to State Farm's discretionary right to grant the Agents permission to place rejected business with other insurance carriers, which is contained in the Principal Occupation Provision. The Agents, however, have not asserted any actionable allegations showing that State Farm refused permission in bad faith.

II Case No. 02-16452 -- The Agents' Appeal From the District Court's Dismissal of Their Independent Action for Failure to State a Claim

We review de novo a dismissal for failure to state a claim pursuant to Federal Rule of Civil Procedure 12(b)(6). *Lipton v. PathoGenesis Corp.*, 284 F.3d 1027, 1035 (9th Cir. 2002). However, an independent action to set aside a prior judgment is based on equity. *In re Levander*, 180 F.3d 1114, 1118 (9th Cir. 1999). We review a district court's decision to deny equitable relief for an abuse of discretion. *Levi Strauss & Co. v. Shilon*, 121 F.3d 1309, 1313 (9th Cir. 1997).

[12] Federal Rule of Civil Procedure 60(b) preserves the district court's right to hear an independent action to set aside a judgment for fraud on the court. An independent action to set aside a judgment for fraud on the court is "reserved for those cases of injustices which, in certain instances, are deemed sufficiently gross to demand a departure from rigid adherence to the doctrine of res judicata." *United States v. Beggerly*, 524 U.S. 38, 46 (1988) (internal quotation marks omitted). "[A]n independent action should be available only to prevent a grave miscarriage of justice." *Id.* at 47 (holding that allegations that the prevailing parting failed during discovery in the underlying case to "thoroughly search its records and make full disclosure to the Court" were not fraud on the court).

[13] As we explained in *In re Levander*, the basis for an independent action to set aside a judgment for fraud on the court lies in misconduct that "harm[s] the integrity of the judicial process." 180 F.3d at 1119 (internal quotation marks omitted). We read the term "fraud on the court" narrowly, and apply the following definition:

> "Fraud upon the court" ... embrace[s] only that species of fraud which does or attempts to,

> defile the court itself, or is a fraud perpetrated by officers of the court so that the judicial machinery can not perform in the usual manner its impartial task of adjudging cases that are presented for adjudication.

Id. (internal quotation marks). Non-disclosure, or perjury by a party or witness, does not, by itself, amount to fraud on the court. *Id.* at 1119-20.

[14] Fraud on the court requires a "grave miscarriage of justice," *Beggerly*, 524 U.S. at 47, and a fraud that is aimed at the court. Here, Orrick's actions, even if they did occur as alleged, were aimed only at the Agents and did not disrupt the judicial process because the Agents through due diligence could have discovered the non-disclosure. Even if the non-disclosure worked an injustice, it did not work a "grave miscarriage of justice." Accordingly, we hold that the district court did not abuse its discretion by dismissing the independent action.

CONCLUSION

[15] For the foregoing reasons, we affirm the district court's summary judgment in the breach of contract action, Case No. 00-16521, and its dismissal of the independent action for failure to state a claim, Case No. 02-16452.

AFFIRMED.

B. FLETCHER, Circuit Judge, dissenting:

In the principal suit, I respectfully dissent. I would hold that the district court erred (1) in not applying collateral estoppel against State Farm and (2) in granting summary

judgment in favor of State Farm. In the independent action, I would reinstate the action because the majority construes the circumstances in which a party commits fraud on the court too narrowly. If proved, the agents' allegations against Orrick and State Farm amount to fraud on the court sufficient to support an independent action.

I. Breach of Contract Action

A. Collateral Estoppel

The majority holds that collateral estoppel does not bar relitigation in this case of the identical issue that was decided in *Sandberg v. State Farm Mut. Auto. Ins. Co.*, 182 F.2d 927 (9th Cir. 1999) (table) (memorandum disposition). *Sandberg* held that, under California law, the contract provisions that are at issue here permit termination only for good cause. The majority concedes that the district court erred in holding that the preconditions for estoppel were not met in this case, *see* majority opinion, *supra*, but the majority nonetheless defers to the district court's ultimate decision not to estop State Farm from relitigating the issue. The majority errs.

To decide as it does, the majority must rely on the exception that "[a]llowing offensive collateral estoppel *may* ... be unfair to a defendant if the judgment relied upon as a basis for the estoppel is itself inconsistent with one or more previous judgments in favor of the defendant." *Parklane Hosiery Co., v. Shore*, 439 U.S. 322, 331 (1979) (emphasis added). We do not apply a mechanical approach to the question of when prior inconsistent judgments preclude the application of collateral estoppel. Instead, we have held that *Parklane Hosiery* is a guide to determining when the application of collateral estoppel may be unfair to a defendant. *See Robi v. Five Platters, Inc.*, 838 F.2d 318, 330 (9th Cir. 1988) ("We prefer to read *Parklane* as providing guidance to the district courts for the appropriate

exercise of discretion as to when to apply offensive issue preclusion in the presence of inconsistent judgments.").

Although *Sandberg* decided that State Farm had good cause to terminate the agent in that case, it held that under California law the same termination clause that is at issue here permitted termination only for good cause. The majority's conclusion that *Sandberg* is "inconsistent" with other authority so as to preclude applying collateral estoppel against State Farm is simply wrong. To be inconsistent in this sense, a decision must conflict with relevant legal authority on the same issue.

This case involves two groups of plaintiffs: (1) those from Arizona, California, Colorado, Iowa, Maryland, Nevada, Utah, and Washington -- states that the district court held follow a rule that permits extrinsic evidence to be used to illuminate the meaning of *unambiguous* contract terms; and (2) those plaintiffs from Florida, Idaho, Kansas, Louisiana, Nebraska, Ohio, and Texas -- states that the district court held permit the introduction of extrinsic evidence if a contract term in *ambiguous*. Neither party has challenged the district court's conclusions in this regard. Accordingly, the only authority that would be relevant in determining that *Sandberg* was "inconsistent" would need to be authority interpreting the rule of law that we applied in *Sandberg* -- that is, authority applying California law, or the law of a state that follows the same rule.

The pre-*Sandberg* authorities that State Farm proffers applied New Hampshire, law, Illinois law, New Mexico law, and Kansas law -- none of which is at issue here (except Kansas). Although State Farm cites three cases from California courts, two are from trial courts, and none of them is California Supreme Court authority. It is wrong to hold, on such a basis, that *Sandberg* is "inconsistent" with the law of California and of the other states that follow the same rule. Nor do any of the

authorities that post-date our decision in *Sandberg* indicate that *Sandberg* is inconsistent.

Moreover, the majority is wrong to defer to the district court's decision in disregarding *Sandberg*. The district court has no such discretion, and we owe the district court's decision on this point no deference. The district court held that our decision in *Sandberg* was sufficiently inconsistent with prior decisions *in other jurisdictions* (not our court) that it would be unfair to estop State Farm from relitigating the scope of the termination clauses at issue. In such circumstances, the lower court's refusal to follow a decision of this circuit is reversible error.

The question of the consistency of *Sandberg* with prior decisions -- and, hence, in some sense *Sandberg*'s fairness -- was a matter for the panel that decided that case. It is improper to assume that the *Sandberg* panel was unaware of, or disregarded, the state of the law when it issued its disposition. Moreover, State Farm had amply opportunity to challenge the consistency (and fairness) of our decision with prior authority when it petitioned for rehearing by the original panel. State Farm again had the chance to raise the issue in its petition for certiorari that was denied by the Supreme Court. *See Sandberg v. State Farm Mutual Auto. Ins. Co.*, 528 U.S. 1118 (2000) (denying petition for certiorari). I submit that the district court here had no discretion to refuse to follow our *Sandberg* decision because, in the lower court judgment, our decision did not agree with prior judgments from different courts.[1]

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1 The district court considered *only* authority prior to *Sandberg* in concluding: "The Court ... takes note of the stark landscape of inconsistent prior interpretations of the termination clause, and finds that this factor weighs heavily in favor of granting *Sandberg* no preclusive effect." The

(continued...)

Nothing in *Parklane Hosiery* suggests that the Supreme Court intended to upset the usual channels of appellate review or to grant discretion to district courts to refuse to accord preclusive effect to prior judgments of their circuit courts. Nor does *Parklane Hosiery* suggest that we should defer to an inferior court within our jurisdiction as to the correct legal application of our own decisions. *Parklane Hosiery* involved the question of whether to grant preclusive effect to a decision by the Second Circuit in a case that was before a district court within the same circuit. *See Id.* at 324-25. But the Supreme Court did not reach the actual question presented here of whether a district court may disregard a prior decision by the court of appeals that sits above it on the ground that the circuit's decision conflicts with foreign authority. Although the Court noted that a general exception might be made for decisions that are inconsistent with prior decisions, it held that "none of the circumstances that might justify reluctance to allow the offensive use of collateral estoppel is present." *Id.* at 331.

The district court has no special expertise nor license to assess, as a matter of law, whether our decisions are right, wrong, consistent, or inconsistent. That is, quite simply, our task (and that of the Supreme Court). Our decisions, whether memorandum dispositions or opinions, state the law of the circuit and must be followed by a district court in cases where they properly govern the issues presented. *See* Ninth Circuit Rule 36-3. The district court had no authority to disregard our decision.

In short, the district court's decision that State Farm is not collaterally estopped from relitigating whether the contracts

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(...continued)
district court's decision amounts to nothing more than an expression of disagreement with the correctness of the *Sandberg* decision.

here are terminable for cause was reversible error. The district court may not disregard our decision, and the conclusion that *Sandberg* is inconsistent with the weight of authority from other jurisdictions on the questions presented in this case is inaccurate.

B. Summary Judgment

I also disagree with the majority that summary judgment was proper. I would reverse and remand for trial. In affirming the grant of summary judgment, the majority ignores the settled standard for summary judgment and substitutes its own interpretation of the evidence for one that views the evidence in the light most favorable to the nonmoving party. At summary judgment, the court is prohibited from taking such a view of the evidence. *See Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986).

Neither party disputes that extrinsic evidence may be used to illuminate and interpret the meaning of the contract terms that are at issue here -- at least as to the plaintiffs who have stated claims for breach of contract under the law of states, such as California, that permit such evidence to be used to interpret unambiguous contract terms. *See, e.g., Pacific Gas and Elec. Co. v. G.W. Thomas Drayage & Rigging Co.*, 442 P.2d 641, 644-47 (Cal. 1968) (en banc). The plaintiffs allege that the deletion of the "at will" provision from a previous version of the agency agreement, the addition of a termination review procedure, and State Farm documents that state that State Farm would not terminate agents except for serious infractions require a holding that the contract permits termination only for cause. Read together, this evidence, considered in the light most favorable to the plaintiffs, clearly supports the reasonable interference that the agency contracts

were terminable only for cause.[2] At summary judgment the plaintiffs need show no more in order to proceed to trial.

The majority is wrong to hold that what the plaintiffs ask us to do is to write in or "graft" onto the contract a "for cause" provision. All that is required for the plaintiffs to prevail at this stage of the case is to present evidence (that we must view in the light most favorable to the plaintiffs) that raises a disputed issue of material fact as to the meaning of the contract. That they have done.

Of course, because the contracts, considered in the light most favorable to the plaintiffs, reasonably may be read to allow termination only for cause, the district court's rulings that State Farm breached no implied covenants of good faith and fair dealing as to the agents' other claims should be reversed as well.

II. The Independent Action

The gravamen of the plaintiff's complaint in the independent action under Rule 60(b) is that State Farm's counsel, Orrick, Herrington & Sutcliffe, committed fraud upon the court by responding to the plaintiffs' request to depose

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2 The district court dismissed much of the evidence that the plaintiffs proffered because it was written after the contract provisions at issue were drafted. The court reasoned that because the evidence postdated the drafting process it lacked any nexus to the drafting and could not illuminate the meaning of the contract provisions. Although such an inference, if justified, could be drawn after trial, it is not permissible at the summary judgment stage. It is entirely possible that the materials that were written after the contract provisions are evidence of what the parties to the contract intended by its provisions.

Henry Keller, a former State Farm executive, by fraudulently claiming to represent Keller and opposing the disposition on grounds that he was very elderly, had long been retired, and possessed no documents or knowledge concerning the subject matter of the lawsuit. In reliance on Orrick's representations, the plaintiffs claim, Orrick did not represent Keller and knew Keller possessed material evidence that strongly supported their claims and was willing and ready to testify.

The majority holds, that Orrick's acts are not actionable because they do not rise to the level of fraud on the court or work a grave miscarriage of justice. I cannot agree. The majority's interpretation as to when a federal court may set aside a judgment is too narrow. Rule 60(b) permits a court, within a reasonable time, not more than one year after a judgment is entered, to grant a motion for relief from a judgment because of, inter alia, fraud on the court. *See* Fed. R. Civ. P. 60(b). After a year elapses, the rule also allows a party to bring an independent action to set aside a judgment for fraud on the court. The power to grant relief in an independent action is based in the court's inherent "power to vacate judgments on proof that a fraud on the court has been committed." *In re Levander*, 180 F.3d 1114, 1118 (9th Cir. 1999) (citing *Chambers v. NASCO, Inc.*, 501 U.S. 32, 43-44 (1991)). Rule 60(b) largely codified preexisting substantive law regarding the circumstances in which courts are empowered to set aside judgments, but removed many procedural complexities that were associated with preexisting law. *See Averbach v. Rival Mfg. Co.*, 809 F.2d 101, 1020-21 (3rd Cir. 1987) (discussing the relationship of Rule 60(b) to prior law and practice). The period of a year specified by Rule 60(b) supplanted the earlier requirement that a request to set aside a judgment that was brought as part of the original action must have been made before end of the term of the court in which the judgment was entered. However, nothing in the text of Rule 60(b) requires

that a plaintiff make a higher showing for relief in an independent action than in a motion under the rule.

The question presented here is whether the fraud that the plaintiffs have alleged may, if proved, warrant relief. Fraud in the discovery process plainly may sustain an independent action under Rule 60(b). The Supreme Court has held that federal courts may set aside judgments, notwithstanding the defense of laches or the plaintiff's lack of diligence in pursuing relief if a judgment has been obtained based on evidence that counsel has "manufactured." *See Hazel-Atlas Glass Co. v. Hartford-Empire Co.*, 322 U.S. 238 (1944). The Third Circuit has held that a plaintiff stated a claim for relief in an independent action based on opposing counsel's false and misleading answers to interrogatories. *See Averbach*, 809 F.2d at 1017, 1022-23. None of our precedents warrants a different result. In *Levander*, we stated that "non-disclosure by itself does not constitute fraud on the court" that warrants relief in an independent action under Rule 60(b), *Levander*, 180 F.3d at 1119, and that ordinary perjury similarly is not actionable, but we explicitly embraced a definition of fraud on the court that encompasses "fraud perpetrated by officers of the court so that the judicial machinery cannot perform in the usual manner its impartial task of adjudging cases." *Id.* at 1119 (quoting 7 James W. Moore, et., Moore's Federal Practice ¶ 60.33, at 515 (2nd Ed. 1978)).

Here, Orrick is alleged not merely to have failed to disclose material evidence[3] that under long-established federal law it was obligated to disclose, but also to have claimed to represent a potential witness that it did not represent and intentionally to have misrepresented that person's position in a calculated attempt to obtain a judgment in its client's favor. An attorney in a legal proceeding who fraudulently claims to

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3 Keller himself advised Orrick that he had material evidence to furnish to the plaintiffs.

represent a client whom she or he does not, not only commits a fraud against the parties to the proceeding, but also a fraud on the court. Both the court and the parties are entitled to rely on an attorney's representation that she or he actually represents a client whom he or she claims to represent. A fraudulent misrepresentation about the fact, nature, and scope of an attorney's mandate is not only an ethical breach but a fraud of the highest order that interferes with the machinery of our judicial system. Our adversary system cannot function if attorneys claim to represent individuals that they do not. The majority fails to appreciate the gravity of Orrick's alleged fraud, and errs as a matter of law in holding that an allegation of such fraud may be dismissed for failure to state a claim.

The majority also errs by holding that the plaintiffs could have, with diligence, discovered Orrick's alleged duplicity by insisting on deposing Keller despite Orrick's representations and that the plaintiffs' failure to do so bars their claim. I strongly disagree. First, under *Hazel-Atlas*, the diligence of a party in discovering the alleged basis for setting aside a judgment is not decisive. *See Hazel-Atlas*, 322 U.S. at 246. Moreover, unlike the perjury in *Levander*, Orrick's alleged fraud will not be subject to the rigors of cross-examination in the factfinding process itself: The representation by counsel that he represents a witness and that the witness has no material information is not "testimony" that may be cross-examined. A party is entitled to rely on the representations of adverse counsel regarding such matters.

As a matter of construing the discovery rules, moreover, the principle that the majority embraces, namely that a party may not rely on the plain representations of adverse counsel in the discovery process, is not cynical but unworkable. It requires a party doggedly to pursue discovery notwithstanding opposing counsel's signed certification that such discovery is not warranted, *see* Fed. R. Civ. P. 26(g), on the possible chance that

opposing counsel is committing fraud. The failure of the party seeking discovery to take such action, which itself might violate the discovery rules, by the majority's lights, precludes it from seeking redress if it later discovers that it has been the victim of fraud. I cannot embrace such a view of the law.

Such an interpretation of the discovery rules is not only unconscionable, but flies in the face of the purpose of the rules themselves. As the Rules Advisory Committee has explained, Rule 26 explicitly imposes an affirmative duty "to engage in pretrial discovery in a responsible manner that is consistent with the spirit and purposes of Rules 26 through 37," Fed. R. Civ. P. 26, Advisory Committee Notes, 1983 Amendment, Subdivision (g), and Rule 37(c) permits a district court to sanction a party for making false or misleading discovery disclosures. *See* Fed. R. Civ. P. 37(c). As the Washington Supreme Court has held, the Federal Rules of Civil Procedure explicitly encourage the imposition of sanctions for discovery abuse in part because "a spirit of cooperation and forthrightness during the discovery process is necessary for the proper functioning of modern trials." *Wash. State Physicians Ins. Exch. & Ass'n v. Fissons Corp.*, 858 P.2d 1054, 1077 (Wash. 1993). The court noted that although "[f]air and reasoned resistance to discovery is not sanctionable[,] ... misleading ... responses [are] ... contrary to the purposes of discovery and ... most damaging to the fairness of the litigation process." *Id.* at 1079-80.

The plaintiffs' allegations, if proved, would be most damaging to the ethical standing and professional reputation of any attorney -- and indeed might have severe collateral consequences such as disbarment.[4] The majority minimizes the

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4 The majority does not hold that Orrick and State Farm have not committed the actions as alleged, but

(continued...)

gravity of the plaintiffs' charge and invites similar behavior in the future by holding that such a claim may be dismissed for failure to state a claim in an independent action under Rule 60(b). As Judge Schwarzer has persuasively explained: "Misconduct, once tolerated will breed more misconduct and those who might seek relief against abuse will instead resort to its self-defense." William W. Schwarzer, Sanctions Under the New Federal Rule 11 -- A Closer Look, 104 F.R.D. 181, 205. I would reverse the district court and reinstate the action.

(...continued)
that the plaintiffs may not seek relief under Rule 60(b). Orrick itself could be well-served by trial of the charges. They must be very disturbing to a reputable firm. If untrue, Orrick should welcome the opportunity to disprove them.

APPENDIX B

United States Court of Appeals
FOR THE NINTH CIRCUIT

WILLIAM A. APPLING, JOSEPH J. KELLY, ROBERT BUEHLER, JOHN LLOYD, DARYL MITCHELL, RICHARD PYORRE, JOHN WEIR, GERARD M. VERDI, WILLIAM R. SPARKS, LEONARD D. DOCTOR, JERRY LEE FLANDERS, VERNE WALTON INS., LARRY K. WILSON, MICHAEL C. HARTMAN, DANIEL BRUMFIELD, MARTIN H. LEFTON, DOUGLAS H. PERRY, MATHEW N. PICKETT, JR., JO ANN SEARCY, WILLIAM R. CORNELISON, MARILYN J. CUSIMANO, DENNIS B. FARRELL, ANDREW W. GAINES, DAVID B. GORDON, PAUL JULIAN, INS., ROSANNE SMITH, W. F. 'BILL' BURBANK INSURANCE AGENCY, INC JEAN A. CORMIER, LEE CRAMER INS. AGENCY, INC.	No. 00-16521 D.C. No. CV-97-01569 -MJJ-MEJ Northern District of California, San Francisco ORDER

FRANKLIN DUTTO, JOAN F.)
EHLER, RAYMOND C.)
GILMORE, ALLEN K.)
GOLDEN, RICHARD O.)
JOHNSON, GABRIEL O.)
JUAREZ, JR., BOB KENNEDY)
INS. AGENCY, INC., LEWIS)
INS. AGENCY, INC., LYKKE)
INS. AGENCY, INC., ROBERT)
G. MARSHALL, TERRY L.)
McMANUS, ALAN L.)
PERKINS, DALE W. PITNEY,)
JR., ELEANOR ROWLAND,)
JORGE SOTELO INS.)
AGENCY INC., ANTHONY E.)
VITO, TERRY D. WALKER,)
JUDY E. WELDIN-)
LEATHERS, THOMAS A.)
WILSON, MICHELLE B.)
PIERCE, aka MICHELLE B.)
YATES, CLIFFORD K.)
YOUNG, WILLIAM)
BATCHELDER, HOOPER INS.)
AGENCY, HAROLD R.)
LITTLE, FRED LOVE, SAM I.)
MAYEDA, JIM MOORE INS.)
AGENCY, INC., MICHAEL L.)
MORGAN, THE EDWARD)
PIERCE INS. AGENCY, INC.,)
DICK JUGE INS. AGENCY,)
INC., PAUL QUILICI, BILL)
BERNARD INS. AGENCY,)
INC., JACOB CASTROLL,)
REGUERA INS. AGENCY,)
INC., CHAMBERS INS.)
AGENCY, INC., LEE)

SAGHIRIAN, TANA P.)
GLOCKNER, aka Tana P.)
Glockner-Shultz, KENNETH)
CARROLL, RICHARD FRANK)
INS. AGENCY, INC., BOB)
ANDRAS INS. AGENCY, INC.,)
PATRICIA ADKINS INS.)
AGENCY, INC., JOANN)
PERGREM, aka JoAnn)
McWilliams,)
)
Plaintiffs - Appellants,)
)
v.)
)
STATE FARM MUTUAL)
AUTOMOBILE INSURANCE)
COMPANY; STATE FARM)
FIRE AND CASUALTY)
COMPANY; STATE FARM)
LIFE INSURANCE)
COMPANY; STATE FARM)
GENERAL INSURANCE)
COMPANY,)
)
Defendants - Appellees.)

WILLIAM A. APPLING;)
LEONARD D. DOCTOR;)
JERRY LEE FLANDERS;)
LARRY K. WILSON;)
MICHAEL C. HARTMAN;)
DANIEL BRUMFIELD;)
MARTIN H. LEFTON;)

DOUGLAS H. PERRY; JO ANN SEARCY; WILLIAM R. CORNELISON; MARILYN J. CUSIMAN; DENNIS B. FARRELL; ANDREW W. GAINES; DAVID B. GORDON; ROSANNE SMITH; PAUL JULIAN INSURANCE AGENCY, INC.; VERNE WALTON INSURANCE AGENCY, INC.; RAYMOND C. GILMORE; BOB KENNEDY INSURANCE AGENCY, INC.; LEWIS INSURANCE AGENCY, INC.; DALE W. PITNEY, JR.; ANTHONY E. VITO; TERRY D. WALKER; PAUL QUILICI; JACOB CASTROLL,	)	No. 02-16452
Plaintiffs-Appellants,	)	D.C. No. CV-01-03181-MJJ
v.	)	Northern District of California, San Francisco
ORRICK, HERRINGTON & SUTCLIFFE; STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY; STATE FARM FIRE AND CASUALTY COMPANY; STATE FARM LIFE INSURANCE COMPANY; STATE FARM GENERAL INSURANCE COMPANY,	)	ORDER
Defendants-Appellees.	)	

Before: B. FETCHER, KOZINSKI, and TROTT, Circuit Judges.

Judges Kozinski and Trott have voted to deny the petition for rehearing and Judge B. Fletcher has voted to grant the petition for rehearing.

Judges Kozinski and Trott have voted to deny the petition for rehearing en banc and Judge B. Fletcher has recommended to grant the petition for rehearing en banc.

The full court has been advised of the suggestion for rehearing en banc and no judge of the court has requested a vote on it. Fed. R. App. P. 35(b).

The petition for rehearing and the petition for rehearing en banc are DENIED.

APPENDIX C

Rules for the United States Court of Appeals for the Ninth Circuit

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CIRCUIT RULE 36-3. CITATION OF UNPUBLISHED DISPOSITIONS OR ORDERS

(a) Unpublished dispositions and orders of this Court are not binding precedent, except when relevant under the doctrine of law of the case, res judicata, and collateral estoppel.

Supreme Court, U.S.
FILED
04 54 JUN 8 - 2004
OFFICE OF

No. _____

IN THE
SUPREME COURT OF THE UNITED STATES

WILLIAM A. APPLING, et al.,
Petitioners,

v.

STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY, et al.,
Respondents.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

SUPPLEMENTAL APPENDIX FOR WRIT OF CERTIORARI

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June 08, 2004

Counsel for Petitioner

APPENDIX D

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

WILLIAM APPLING, et al.,	)	No. C 97-1569 MJJ
	)	
Plaintiffs,	)	**ORDER DENYING**
	)	**PLAINTIFFS' MOTION**
v.	)	**FOR PARTIAL**
	)	**SUMMARY**
STATE FARM MUTUAL	)	**JUDGMENT AND**
AUTOMOBILE INSURANCE	)	**GRANTING**
CO.,	)	**DEFENDANTS'**
	)	**COUNTERMOTION**
Defendant.	)	**FOR PARTIAL**
	)	**SUMMARY**
_____/	)	**JUDGMENT**

INTRODUCTION AND FACTUAL BACKGROUND

Before the Court are the parties' cross-motions for partial summary judgment. Plaintiffs (collectively "Appling") move for partial summary judgment on the termination provision of the State Farm employment contracts, which State Farm contends allow termination of the contract at will, and Appling contends can be terminated only for cause. Appling relies on the unpublished Ninth Circuit disposition in *Sandberg v. State Farm*, No. 97-55971 (May 13, 1999), finding that the State Farm agent employment contract was susceptible to a good cause termination reading, as collateral estoppel from relitigating the contractual interpretation issue in this case. State Farm contests *Sandberg's* entitlement to collateral estoppel effect on several bases, and has countermoved the Court for the determination that the employment contracts are

integrated and unambiguously provide that employment is terminable at will.

Appling's motion implicates a subset of 28 of the agent plaintiffs, all of whom have been terminated as State Farm agents for a variety of alleged transgressions, including, *inter alia*, eliciting improper matching contributions from the State Farm Foundation and refusing to attend mandatory training sessions. Specifically, Appling moves for summary judgment on count 3 of the Sixth Amended Complaint, counts 12 and 14 of the Gilmore/Walker and Castroll/Lewis supplemental complaints, and count 1 of the Pyorre/Wier supplemental complaints. Assuming *arguendo* the failure of their collateral estoppel argument, Appling argues in the alternative that extrinsic evidence demonstrate that the contract was terminable only upon good cause, and thus that a breach of covenant claim may lie against State Farm.

State Farm's counter-motion would eliminate the terminated agents' breach of implied covenant claims of the terminated agents, implicating counts 3, 4 and 5 of the Sixth Amended Complaint, counts 12, 13 and 14 of the Castroll/Lewis supplemental complaint, counts 17, 18 and 19, of the Gilmore/Walker supplemental complaint, and counts 1, 2 and 3 of the Pyorre/Wier supplemental complaint. The contracts at issue (the AA3, AA4 and AA660)[1] all provided specific language regarding the termination of the contract. For the agent contracts, the relevant language reads: "You or State Farm have the right to terminate this Agreement by written notice delivered to the other or mailed to the other's last known address." AA3 and AA4 Agreements, section III(A); AA660

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1 Eighteen plaintiffs sue under the AA3 agreement (agent or corporate form), nine under the AA4 agreement, and one under the AA660 agreement. (Brick Decl., Exh. J).

Agreement, section III(1). The corporate versions of these same agreements provide similar language. All of the contracts at issue also provide that the written agreements supersede all prior written and oral representations between the parties, and incorporate an integration clause which reads: "This Agreement constitutes the sole and entire agreement between the parties hereto, and no change, alteration, or modification of the terms of this Agreement may be made except by agreement in writing signed by an authorized representative of the Companies and accepted by you." AA3 and AA4 Agreements, section VI(E); AA660 Agreement, section V(5). The agent contracts feature a termination review clause, whereby any terminated agent is guaranteed the ability to contest the basis for his or her dismissal by petitioning a regional board and, ultimately, to have the termination reviewed by the President of the company. AA3 Agreement, section III.B; AA4 Agreement, section III.B; AA660 Agreement, section III.2. The corporate version of the contracts does not include the termination review guarantees.

LEGAL ANALYSIS

I. Appling's Motion

A. Legal Standard

In invoking the *Sandberg* decision, Appling seeks to use the doctrine of offensive collateral estoppel to foreclose the Court's inquiry into the meaning of the termination clause provision. Offensive collateral estoppel permits a plaintiff in a subsequent litigation to foreclose litigation of a given issue, where that issue has been decided against the same defendant in a prior judgment. In *Parklane Hosiery v. Shore*, 439 U.S. 322 (1979), the Supreme Court Found that despite the traditional requirement of mutuality in applying collateral estoppel, the doctrine was appropriate in certain, non-mutual circumstances. *Parklane Hosiery* emphasizes that the trial

court is accorded broad discretion in determining when and how collateral estoppel is to apply. 439 U.S. at 331. *Parklane Hosiery* notes that offensive collateral estoppel does not promote judicial economy in the same manner as defensive collateral estoppel does. *Id.* at 329. The Court noted several scenarios illustrating the potential for unfairness in wooden application of offensive collateral estoppel. *Id.* at 329. The Court noted several scenarios illustrating the potential for unfairness in wooden application of offensive collateral estoppel. *Id.* at 330-331. Among them was a scenario whereby "the judgment relied upon as a basis for the estoppel is itself inconsistent with one or more previous judgments in favor of the defendant." *Id.* at 330.[2] The Ninth Circuit has reemphasized *Parklane Hosiery's* teaching that applications of offensive collateral estoppel is within the broad discretion of the trial court. *See, e.g., Robi v. Five Platters*, 838 F.2d 318, 329-330 (9th Cir. 1988). With these discretionary principles in mind, the Court turns to a consideration of the relevant factors in the context of *Sandberg*.

B. The *Sandberg* Opinion

Last year, a Ninth Circuit panel issued an unpublished memorandum affirming summary judgment in favor of State

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2 Professor Currie's hypothetical railroad collision, explained in footnote 14 of *Parklane Hosiery*, 439 U.S. at 330, illustrates this point. Were a train carrying 50 passengers to derail, and passengers 1 through 26 all individually unsuccessful in holding the railroad liable for negligence, Professor Currie opines that a favorable judgment for passenger 27 should not entitle passengers 28 through 50 to prevail as a matter of estoppel. While prior judicial interpretations on this issue are not so numerous, they were, prior to *Sandberg*, unanimous. *See infra*.

Farm in a wrongful termination case. *Sandberg v. State Farm*, No. 97-55971 (May 13, 1999). In that case, Sandberg (a State Farm policy holder policyholder as well as an agent) was terminated after he brought a suit for fraud against State Farm on his own policy, seeking punitive damages. The Ninth Circuit undertook a two-part, *de novo* analysis of the contractual interpretation of termination language, following *Brinderson-Newberg Joint Venture v. Pacific Erectors*, 971 F.2d 272, 277 (9th Cir. 1992). Under the test, the Court first affirmed the district court's finding that the contract was fully integrated. Slip Op. at 3. The court then moved on to analyze the termination provision. It relied explicitly on two sources of extrinsic information supporting Sandberg's argument that the agreement was terminable only for cause: (1) the previous agency agreement, which had provided that termination was possible "with or without cause", had been modified to omit the quoted term; and (2) a 1977 article by State Farm's vice president that asserted that the termination review procedure would ensure that termination would occur only when the file "clearly supports a serious violation of a contract agreement" Slip Op. at 3-4.

From this extrinsic evidence, the Court parted company with the district court's conclusion, and found: "Viewing the evidence most favorable to Sandberg, we hold that the agreement is reasonably susceptible to a termination-for-cause interpretation."[3] Slip Op. at 4. In support of this conclusion, the *Sandberg* court cited to three cases (*Wallis v. Farmers Group, Inc.*, 269 Cal.Rptr. 299, 306-7 (1990), *Jack Rowe Associates, Inc. v. Fisher Corp.*, 833 F.2d 177, 181 (9th Cir. 1987), and *Sherman v. Mutual Benefit Life Ins. Co.*, 633 F.2d 782 (9th Cir. 1980)) interpreting California law to allow oral or other extrinsic evidence to modify an otherwise at-will termination

provision. The Court cited no case interpreting the State Farm termination clause to be at will.

The Ninth Circuit ultimately affirmed the district court's holding, however, since it found that the basis for Sandberg's termination constituted good cause. "While we agree with Sandberg's interpretation that the agency agreement limited termination to good cause, we hold that Sandberg's claim for punitive damages is sufficient 'good cause' to support State Farm's decision to terminate." Slip Op. at 5. Thus, *Sandberg's* affirmance of the district court judgment does not rely directly on its disagreement with the district court's finding of at will termination, and would have arrived at the same conclusion even had it agreed.

C. State Farm's Attacks on Collateral Estoppel

State Farm urges the Court to utilize its discretion to disregard its potentially preclusive effects of *Sandberg* as collateral estoppel on all four prongs of the *Parklane Hosiery* test. Specifically, State Farm alleges: (1) Sandberg's finding on the termination clause provision was contrary to previous court treatments of the same issue, and thus would be unfairly relied upon for its preclusive effect; (2) the finding itself was not a fully and necessarily litigated part of the judgment, in that the opposite determination would not have altered the ultimate holding reached; (3) since State Farm actually prevailed on the merits of the decision, preclusion against it would be legally inappropriate; and (4) amplifications in the relevant state law occurred after submission, and prevented a full and fair opportunity to litigate the interpretation issue.

The Ninth Circuit Rules provide that the *Sandberg* memorandum is to be given collateral estoppel effect, or otherwise be completely disregarded. Rule 36-3 prohibits the

citation to or reliance upon unpublished dispositions of the Ninth Circuit unless they are given preclusive effect.[4] Accordingly, the Court must disregard the memorandum entirely in its determination of the merits of this case, if it should deny collateral estoppel based on the *Sandberg* memorandum

1. Holding Contrary to Prevailing Law

There is no argument that *Sandberg* represents the first and only of several Court rulings on the State Farm agent agreement termination clause interpretation issue to find that the language was even susceptible to a good cause termination reading. All other courts considering the effect of the State Farm contractual termination provisions have reached the opposite conclusion. *Mooney v. State Farm*, 344 F.Supp. 697 (D.N.H. 1972); *Vitkauskas v. State Farm*, 509 N.E.2d 1385 (Ill. App. Ct. 1987); *Melnick v. State Farm*, 106 N.M. 726 (N.M. 1988); *Drum v. State Farm*, S. F. Superior Ct. Case No. 991165 (Nov. 30 1998) (Req. Jud. Not., Exh. A); *Lotten v. State Farm*, Contra Costa Superior Ct. Case No. 97-01951 (July 30, 1998) (Req. Jud. Not., Exh. B); *Peters v. State Farm*, Case No. 82-2177-S (D. Kan. 1996) (Req. Jud. Not. Exh. C); *Scola v. State Farm*, Case No. 1-49685 (1st Dist. 1981) (Req. Jud. Not., Exh. D). On the other hand, Appling contends that *Sandberg* is consistent with *Wallis*, and is thus appropriately relied upon as an articulation of California law.

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4 Rule 36-3 reads: "Any disposition that is not an opinion or an order designated for publication under Circuit Rule 36-5 shall not be regarded as precedent and shall not be cited to or by this Court or any district court of the Ninth Circuit, either in briefs, oral argument, opinions, memoranda, or orders, except when relevant under the doctrines of law of the case, res judicata, or collateral estoppel."

The Ninth Circuit has confirmed that the fairness principles outlined in *Parklane* are particularly acute where the judgment asserted is inconsistent with prior rulings in favor of the defendant. *See Robi*, 838 F.2d at 330. In the District of Columbia Circuit, inconsistency of prior judgments alone is a basis for denying the application of offensive collateral estoppel. *Jack Faucett Assocs. v. American Telephone & Telegraph Co.*, 744 F.2d 118, 125-6 (D.C. Cir. 1984). While the law is not so categorical in this Circuit, it is clear under *Parklane Hosiery* that a ruling at odds with prior judicial determinations of the same factual issue presents questions of fundamental fairness to the defendant. The Court, accordingly, takes note of the stark landscape of inconsistent prior interpretations of the termination clause, and finds that this factor weighs heavily in favor of granting *Sandberg* no preclusive effect. Because that determination alone is not enough to resolve the question, the Court moves on to the other *Parklane Hosiery* factors.

2. Finding For Which Estoppel is Sought Unnecessary to Holding

State Farm's second argument is that the finding that the contractual provision was a good cause termination provision was not necessary to the judgment. Necessity to the underlying judgment is a prerequisite under *Parklane Hosiery* for invoking offensive collateral estoppel. *Carter v. U.S.*, 973 F.2d 1479, 1482 (9th Cir. 1992.). The Ninth Circuit has found this to be the case for subsidiary factual holdings adverse to a prevailing party. *See, e.g., U.S. v. Good Samaritan Church*, 29 F.3d 487 (9th Cir. 1994). *Good Samaritan* is instructive on this point. There, the appellant had won below on a quiet title action against the IRS. In reaching its holding on title, the district court found that Good Samaritan was the alter ego of the trasnferor of title. Citing *Montana v. U.S.*, 440 U.S. 147, 153 (1979), the Ninth Circuit held that for issue preclusion to operate, the alter ego determination would have had to be

necessarily determined in the district court decision. "The district court dismissed the government's case because the government did not give proper notice. It could have reached that decision regardless of how the alter ego issue came out, or without reaching the alter ego issue at all." 29 F.3d at 489. The court concluded that the alter ego issue was not precluded from relitigation, and dismissed Good Samaritan's appeal.

In this case, the *Sandberg* court's finding that the State Farm contract was susceptible to a for-cause termination standard was not necessary to its ultimate affirmance. In fact, as in *Good Samaritan*, the *Sandberg* court could have reached the opposite conclusion on the contractual interpretation issue without affecting its ultimate affirmance. In these circumstances, there is a compelling basis for denying preclusive effect to a finding subsidiary to, and unnecessary to, the holding.

U.S. v. Weems, 49 F.3d 528 (9th Cir. 1995), which Appling relies upon to rebut this point, is not really at odds with State Farm's position. *Weems* granted collateral estoppel effect to the previous determination that the defendant was an innocent owner of property in a civil forfeiture proceeding in the subsequent criminal trial. After reiterating that only findings necessary to the judgment were the proper basis for collateral estoppel, *Weems* held that the prior ruling was, in that the finding changed the statutory basis under which the forfeiture should be sought. Thus, *Weems* on its facts does State Farm's arguments little harm.

3. Preclusive Effect of Harmful Findings in Favorable Judgment

The *Parklane Hosiery* standards as interpreted by Ninth Circuit requires that the intended preclusive finding be made in a decision adverse to the party against whom preclusion is subsequently sought. *Pena v. Gardner*, 976 F.2d 469, 472 (9th

Cir. 1992).[5] One rationale for this requirement is that a prevailing party has no ability to appeal that portion of the judgment it is affected by, and thus appellate review is thwarted. The Ninth Circuit has refused to review a positive district court judgment with subsidiary negative findings for the appellant on just this basis. *See, e.g., Fireman's Fund Ins. Co. v. International Market Place*, 773 F.2d 1068 (9th Cir. 1985). Since State Farm would not have had the ability to appeal the portion of the *Sandberg* order, at a general level, the point is availing. This rationale is perhaps weakened in that the precluding court is a court of appeal, not a district court, and thus no "right of appeal" would entail even for adverse judgments.

4. Full and Fair Litigation of the Issue Decided

State Farm's analysis on this issue pertains to the timing and consideration of the *Bionghi* decision, which it claims would have led the Ninth Circuit to a different result under California contract interpretation law, relative to the *Sandberg* argument and order. *Sandberg* was argued and submitted on February 1, 1999. *Bionghi* was decided on March 30, 1999, and submitted for the panel's attention without comment by State Farm, pursuant to F.R.A.P. 28(j). The *Bionghi* decision is mentioned nowhere in the *Sandberg* disposition, filed on May 13, 1999. In its petition for rehearing, State Farm argued the importance of *Bionghi*, but the request for rehearing was denied without comment in July. (Doolittle Decl., Exh. R, S).

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5 *But see, e.g., Clark v. Bear Stearns*, 966 F.2d 1318 (9th Cir. 1992), citing the Eleventh Circuit standard, which does not incorporate the "adverse judgment" prong of the collateral estoppel test.

Upon this timeline, State Farm contends that it was denied a full and fair opportunity to litigate the contract interpretation issue. Appling counters that the submission of *Bionghi*, and the panel's implicit consideration of the case, without argument in the initial stage and with vigorous argument in the rehearing petition stage, means that the issue was fully and fairly litigated and thus that the Court's denial of preclusion based on *Bionghi* would be improper. The Court finds that Appling has the better of the argument on this point. While *Bionghi* is not explicitly mentioned or tacitly distinguished in the *Sandberg* memorandum, the Court is unwilling to draw the stark interference urged by State Farm, *i.e.*, that the case was improperly ignored by the panel. Mere omission of this single appellate court case from the written opinion is not enough to support the conclusion that State Farm was denied a full and fair opportunity to litigate the issue in *Sandberg*.

After weighing of all of the factors identified by *Parklane Hosiery* and its Ninth Circuit progeny, the Court finds that the unfairness to State Farm of holding *Sandberg* against it as collateral estoppel outweighs any benefits or efficiencies that collateral estoppel might yield here. Therefore, the Court exercises its discretion by declining to give *Sandberg* collateral estoppel effect in regard to the interpretation of the termination clause in the State Farm contracts at issue. Accordingly, under Circuit Rule 36(3), the Court is bound not to cite or rely on *Sandberg* in its determination of the issues.

II. The Parties' Motions Regarding Termination Standard

I. Contract Interpretation

A. Legal Standards

In *Pacific Gas & Electric v. G.W. Thomas Drayage*, 69 Ca.2d 33 (1968), the California Supreme Court set out the rules governing the use of parol evidence in contract interpretation. *P G&E* makes clear that extrinsic evidence has a role in contract interpretation, even where the term to be construed is integrated. In so doing, *P G&E* forbids courts from truncating an inquiry where it determines that the contractual language at issue has a plain meaning. Specifically, *P G&E* envisions a two-part inquiry to be undertaken prior to evaluating the proper role of extrinsic evidence. First, the reviewing court must look to the contract and see if its is integrated. Where it is, as here, the Court's second inquiry is whether the contractual language is "reasonably susceptible" to the meaning urged upon it by the movant. In so doing, the reviewing court may consider extrinsic evidence "so that the court can place itself in the same situation in which the parties found themselves at the time of contracting. If the court decides, after considering this evidence, that the language of a contract, in the light of all the circumstances, 'is fairly susceptible of either one of the two interpretations contended for...' extrinsic evidence relevant to prove either of such meanings is admissible." 69 Cal.2d at 39-40. Where the contractual language is not deemed capable of alternative meanings after this limited consideration of the extrinsic evidence, a court may proceed.

Courts have subsequently cautioned against overutilization of extrinsic evidence under *P G&E,* particularly urging that the parol evidence rule, codified by statute (Code Civ. Proc. § 1856), not suffer in its wake. "[The *P G&E* rule] must be restricted to its stated bounds; it does no more than

allow extrinsic evidence of the parties' understanding and intended meaning of the words used in their written agreement. While it allows parol evidence for this purpose, it is unconcerned with collateral agreements." *Brawthen v. H&R Block*, 28 Cal.App.3d 131, 136 (1972). *Bionghi* states the issue even more sharply.

> *Pacific Gas and Electric* is thus not a cloak under which a party can smuggle extrinsic evidence to add a term to an integrated contract, in defeat of the parol evidence rule. Instead, it calls for a two-step process. First, the court must determine whether the language of the contract is reasonably susceptible to the meanings urged to show that the parties' understanding of words used differed from the by the parties. In so doing, the court must give consideration to any evidence offered common understanding. If the court determines that the contract is reasonably susceptible of the meanings urged, extrinsic evidence relevant to prove the meaning agreed to by the parties is admissible.

Bionghi, 70 Cal.App.4th at 1365.

Thus, the Court must limit its consideration of the extrinsic evidence in interpreting an integrated contract to give meaning to the contractual language, and not to add, subtract or modify terms in violation of the parol evidence rule.

B. Policy Language

The contracts at issue (the AA3, AA4 and AA660, and its corporate versions) all include specific provisions regarding the termination of the contract. For the individual contracts, the

relevant language reads: "You or State Farm have the right to terminate this Agreement by written notice delivered to the other or mailed to the other's last known address."[6] AA3 and AA4 Agreements, section III(A); AA660 Agreement, section III(1). The corporate versions of these same agreements provide similar language. All of the contracts at issue incorporate an integration clause, which reads: "This Agreement constitutes the sole and entire agreement between the parties hereto, and no change, alteration, or modification of the terms of this Agreement may be made except by agreement in writing signed by an authorized representative of the Companies and accepted by you." AA3 and AA4 Agreements, section VI(E); AA660 Agreement, section V(5).

C. Extrinsic Evidence

Both parties offer extrinsic evidence to support their reading of the relevant contractual term. While this is appropriate under *P G&E* to elucidate the plain meaning of the terms, the Court's role in interpreting this extrinsic evidence is (1) limited to information that would assist in putting the Court in the position of the parties at the time the contract was negotiated, and (2) in the case of an integrated contract, limited to explicating, not varying or adding, existing term language.

As a general point, little of the extrinsic evidence offered by either party strictly adheres to the *P G&E* test, in that none of it is contemporaneous with the negotiation and drafting of the relevant language. Also absent from the record is the testimony of any plaintiff indicating that he or she believed the clause at the time of contracting to provide for termination for

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6 This replaced termination language providing for termination "with or without cause." (Doolittle Decl., Exh. L).

cause. What is set forth instead is largely a battle of the *post hoc* interpretation of the term. With that constraint in mind, the Court now turns to a summary of the extrinsic evidence offered by both sides.

1. Appling's Proffer

Appling offers three broad types of evidence which it claims bear on the question of interpreting the contract's reasonable susceptibility to an interpretation of good-cause termination. First, Appling points to the prior generation of contracts (none of which are at issue here) wherein the term "with or without cause" was included in the termination provisions. (Doolittle Decl., Exh. L.) State Farm removed that term from its standard individual and corporate contracts, inserting in its place a provision allowing termination by either party on written notice. Appling contends that this omission constitutes an abandonment of a strict at-will termination policy. Second, the introduction of a termination review process was instituted, providing the terminated agent an opportunity to air his/her grievance in accordance with procedures established by State Farm's Board of Directors. (Doolittle Decl., Exh. U). Appling asserts that this structure, insofar as it is an affirmative entitlement for employees, is inconsistent with an at-will termination clause. Third, Appling points to comments in employee literature and corporate guidebooks in the wake of the relevant contract revisions made by State Farm executives, indicating that no termination would be effectuated except in the case of serious infractions. Doolittle Decl., Exh. K.

Again, what is lacking in any nexus between this evidence and the contemporaneous, subjective states of mind of any of the agent contractors. Without that critical link, it is difficult if not impossible to envision a scenario by which the contractual terms could be substantially enhanced by reference to this extrinsic evidence. A contracting party cannot be held

to convert what would otherwise be an at-will termination obligation into a for-cause provision by virtue of its own acts to ensure termination occurs only for acceptable reasons. To so hold would risk chilling contracting parties' own efforts to maintain the contractual relationship, lest their own cooperation increase their contractual obligation under an implied-in-fact contract theory. *See, e.g., Davis v. Consolidated Freightways*, 29 Cal.App.4th 354, 367 (1994). Performance and bargained for rights must remain distinct, and can converge only where the extrinsic evidence supports such a unity. It does not here.

2. State Farm's Proffer

For its part, State Farm attempts to show that the terminated agents would have understood that the contract's terms allowed at-will termination. For this, State Farm points to repeated excerpts from agent association newsletters explaining the contracts as at-will. (Brick Decl., Exhs. L, P, Q, R, S, T, V). Also offered are percipient witness testimony for State Farm representatives, who claim that all sides understood at the time the new contract were introduced that a for-cause provision was not incorporated therein. (Joslin, Robinson Decls). Other evidence suggests this understanding inferentially, such as newsletter articles advocating an explicit "just cause" provision in the contract, and expressing fear that the termination review board procedures would protect agents' contractual rights adequately. (Brick Decl., Exhs. M, N, O, R, U, W, Y). Again, the Court bears in mind that much of this proffer is outside of the realm of what *P G&E* would have a reviewing court consider, but that is not to marginalize this proffer entirely. On this record, there lacks a body of extrinsic evidence that would under *P G&E* render the contractual termination language susceptible to a for-cause meaning.

D. State Farm's Motion

State Farm's motion is legally based upon its interpretation upon *P G&E, Masterson v. Sine*, 68 Cal.2d 222 (1968), and the subsequent treatment of those cases in *Bionghi*. State Farm has also pointed to the decisions of a half-dozen different courts construing this identical language to provide for at-will termination. *Mooney v. State Farm*, 344 F.Supp. 697 (D.N.H. 1972); *Vitkauskas v. State Farm*, 509 N.E.2d 1385 (Ill. App. Ct. 1987); *Melnick v. State Farm*, 106 N.M. 726 (N.M. 1988); *Drum v. State Farm*, S.F. Superior Ct. Case No. 991165 (Nov. 30 1998) (Req. Jud. Not., Exh. A); *Lotten v. State Farm*, Contra Costa Superior Ct. Case No. 97-01951 (July 30, 1998) (Req. Jud. Not. Exh. B); *Peters v. State Farm*, Case No. 85-2177-S (D. Kan. 1996) (Req. Jud. Not. Exh. C); *Scola v. State Farm*, Case No. 1-49685 (1st Dist. 1981) (Req. Jud. Not., Exh. D).

For its part, Appling points the Court strongly to *Wallis* for guidance in how to interpret *P G&E*. Clearly, the two appellate decision are in tension. While it is the Court's duty to look to state appellate law for guidance, it cannot do so unambiguously where decisions are at tension with one another, and must resolve the question ultimately as the California Supreme Court would. Ultimately, the Court is spared the task of choosing between *Bionghi* and *Wallis* by the fact that an application of *P G&E* offers the necessary guidance to resolve the motion. *P G&E* cautions the reviewing court against relying on its plain meaning analysis alone to discern the meaning of contract terms. The analysis must begin there, however, and the language seems on its face explicitly to provide an at-will termination provision for either contracting party. The Court must, however, evaluate the extrinsic evidence under *P G&E* to ascertain whether the language is susceptible of meaning other than its literal reading. On this point, Appling's proffered information is of minimized importance as a matter of law. First, on the issue of prior contractual language Appling's

argument relies on the absence of language. The evidence offered nowhere suggests that the omission of the term "with or without cause" essentially means "with cause." On the contrary, State Farm's own in-house memoranda suggest that the contractual term is at will. (*See, e.g.*, Brick Decl., Exh. L). Similarly, meetings held at the time the contracts at issue were introduced to State Farm agents in 1968 and 1976 confirms that the corporation and agent representatives understood the contracts to be terminable at will. (Joslin Decl., Robinson Decl.) Further, and most saliently under *P G&E*, Appling points to nothing in the record to suggest the terminology in the contract meant other than what it says, and has thereafter been interpreted by State Farm and agent representatives to say, to any plaintiff at the time of contracting. Second, as to the establishment of a termination review process under the 1977 amendments, California law suggests that an employer should not be penalized for going the extra step to ensure all terminations are well-based by turning a procedure designed to foster that goal into an affirmative, substantive contractual right. *Davis, supra.* Third, employee bulletins explaining the termination review process as limiting termination to cases of serious contractual violations (Doolittle Decl., Exh. F at 3) do not rise to the level of converting at-will language to for-cause. Again, Appling points to no specific competent evidence in that document that would actually change the reasonably susceptible meaning of the term from at-will to for cause. On the contrary, many of the exhibits offered by Appling permit the opposite conclusion, and that the representatives of the State Farm agents were aware, at least after the fact, that the contracts were, terminable at will. Telling evidence of this is the agents' expressed concerns about inadequate substantive protections in the wake of the 1977 contractual amendments, and a call for an explicit "just cause" provision in future contracts. (Brick Decl., Exhs. M, N, O, R, U, V, Y).

Although the Court is mandated by *P G&E* to focus upon the parties' intent at the time of entering into the contract,

and should not be distracted by the post-contractual interpretations of either side, it is clear that even an charitably overbroad consideration of extrinsic evidence does not help Appling's cause on this point. The Court cannot envision a scenario whereby Appling's proposed interpretation could vary the language of the termination clause. With that conclusion, the Court is bound to accord the language its meaning, and, consistently with several other courts, finds that the language connotes an at-will contractual agency. Accordingly, the Court DENIES Appling's motion for summary judgment of a for-cause interpretation, and GRANTS State Farm's countermotion for summary judgment of a contractual agreement mutually terminable at will.

While the Court's ruling is pursuant to California law, many of the agent plaintiffs are not California residents, and California law has no place in consideration of their claims. The thumbnail overview of foreign law offered by the parties briefs suggests that while some states' contract law fashion a role for extrinsic evidence in interpretation of integrated contracts that is similar, if not functionally identical, to California's, other states utilize the "plain meaning" rule prevalent in California pre-*P G&E*. The Court is unwilling, however, to make wholesale rulings on the state of the law in other jurisdictions in the summary fashion urged by the parties, and therefore limits its ruling on the motion before it to claims arising under California law.[7] However, the parties are

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7 Therefore, the Court's ruling impacts the claims of the following plaintiffs: Appling, Brumfield, Castroll, Cornielson, Cusimano, Doctor, Farrell, Gilmore, Gordon, Julian Insurance Agency, Kennedy Insurance Agency, Lefton, Perry, Pickett, Searcy, Walker, and Walton Insurance Agency. Plaintiffs Pyorre and Wier are not parties to this motion, as the Supplemental Complaints implicating

(continued...)

requested in the interests of judicial economy to confer, and stipulate to the out-of-state plaintiffs whose claims are necessarily impacted by the Court's treatment of the extrinsic and intrinsic evidence in this memorandum and order. A case management conference will be held on February 15, 2000 at 2:00 p.m. to discuss this and other issues further.

CONCLUSION

For the reasons set forth above, Appling's motion for partial summary judgment on the basis of collateral estoppel is DENIED, as is Appling's motion for summary judgment on contractual interpretation of the termination clause. State Farm's countermotion as to the contractual interpretation issue is GRANTED, as the Court finds that the AA3, AA4 and AA660 State Farm agent contracts, and their corporate counterparts, provide as a matter of California law for termination at will by either party.

IT IS SO ORDERED.

Dated: 01/07/2000

/s/
MARTIN J. JENKINS
U.S. DISTRICT JUDGE

(...continued)
their claims was never served on State Farm. Plaintiffs' counsel is reminded of his representation to this Court at oral argument on December 14, 1999 in the now-dismissed *State Farm v. Pyorre and Wier*, Case No. 99-4668 MJJ, that Pyorre and Wier would be dismissed from the case altogether. To date, the civil docket does not reflect any attempt or request to dismiss these plaintiffs from present action.

APPENDIX E

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

WILLIAM A. APPLING, et al.,	)	No. C 01-3181 MJJ
	)	
Plaintiffs,	)	**ORDER GRANTING**
	)	**WITH PREJUDICE**
v.	)	**DEFENDANTS'**
	)	**MOTION TO DISMISS**
STATE FARM MUTUAL AUTO. INS. CO., et al.,	)	**FIRST AMENDED**
	)	**COMPLAINT TO SET**
	)	**ASIDE PART OF**
Defendant.	)	**SUMMARY**
	)	**JUDGMENT IN CASE**
_____/	)	**NO. C 97-1569 MJJ**

INTRODUCTION

Before the Court is a motion to dismiss the first amended complaint pursuant to Federal Rules of Civil Procedure 12(b)(6) brought by Defendants State Farm Mutual Automobile Insurance Company, State Farm Fire and Casualty Company, State Farm Life Insurance Company, and State Farm General Insurance Company (collectively "State Farm"), and Orrick Herrington & Sutcliffe LLP ("Orrick").[1] This motion

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1 Together with the motion, State Farm and Orrick (collectively "Defendants") submit a request for judicial notice of documents referenced in Plaintiff's first amended complaint, and court records in an underlying case. Consideration of such documents does not convert

(continued...)

requires the Court to determine whether Plaintiffs meet the criteria to bring an independent action to set aside part of the summary judgment in a prior matter entitled *William Appling, et al. v. State Farm Mut. Auto. Ins. Co.*, No. CV 97-1569 MJJ ("1997 Action") for fraud upon the court pursuant to Federal Rule of Civil Procedure 60(b).[2] For the following reasons, the Court GRANTS WITH PREJUDICE Defendants' motion.

(...continued)
Defendants' motion into a motion for summary judgment and is proper. *See Lee v. City of Los Angeles*, 250 F.3d 668, 688 (9th Cir. 2001) (finding that courts may consider documents which are not physically attached to the plaintiff's complaint if their authenticity is not contested and the complaint necessarily relies on them); *In re American Continental Corp. Lincoln Savings and Loan Sec. Lit.*, 102 F.3d 1524, 1537 (9th Cir. 1996), *reversed on other grounds by Lexecon, Inc v. Milberg Weiss Bershad Hynes & Lerach*, 520 U.S. 26 (1998) (finding that courts may take judicial notice on "matters of public record, including court records in related or underlying cases which have a direct relation to the matters at issue" without converting the motion into one for summary judgment). In addition, Plaintiffs filed no objections to Defendants' request for judicial notice. As such, the Court GRANTS Defendants' request and considers the documents attached thereto as part of the record in resolving the motion.

2 Rule 60(b) provides, in relevant part, that "this rule does not limit the power of a court to entertain an independent action ... to set aside a judgment for fraud upon the court."

FACTUAL BACKGROUND

In the 1997 Action, Plaintiffs alleged, among other things, that State Farm breached certain of its contracts with the agents who sell State Farm insurance products to customers when it terminated its agents without cause. *See* First Amended Complaint ("FAC") at ¶¶ 9-10. Plaintiffs moved for summary judgment as to the issue of the termination provisions. State Farm brought a counter motion arguing that State Farm had the absolute right to terminate its agents at will and without any cause under the terms of the contract. *See Id. at* ¶ 11; *see also* 1997 Action, slip op. at 1 (N.D. Cal. filed January 7, 2000) ("2000 Order") (stating that "[Defendants] countermoved the Court for determination that the employment contracts are integrated and unambiguously provide that employment is terminable at will.").

Plaintiffs submitted with their motion evidence it claimed went to the question of whether the termination provisions, which provided for termination upon notice, were reasonably susceptible to an interpretation of good-cause termination. First, Plaintiffs pointed to the prior generation of contracts in which the term "with or without cause" was included in the termination provisions. Plaintiffs argued that when State Farm, in 1966, inserted a provision allowing termination by either party on written notice in the place of the "with or without cause" provision, State Farm abandoned its strict at-will termination policy. *See* 2000 Order at 11. Second, Plaintiffs argued that the implementation of a termination review process for its agents by State Farm was inconsistent with an at-will termination clause. *See Id.* Finally, Plaintiffs pointed to comments in employee literature and corporate guidebooks in the wake of the relevant contract revisions indicating that no termination would be effectuated except in the case of serious infractions. *See Id.*

After considering all of the information provided by Plaintiffs, this Court, in its 2000 Order, granted State Farm's motion.[3] *See* FAC at ¶ 12; *see also* 2000 Order at 14. It made its decision after finding that it was "difficult if not impossible to envision a scenario by which the contractual terms could be substantially enhanced by reference to [the extrinsic evidence proffered by Plaintiffs]" because the evidence lacked "any nexus" with the contemporaneous subjective states of mind of the agent contractors. *See* 2000 Order at 11.

On August 20, 2001, Plaintiffs filed the instant action to set aside the 2000 Order, or in other words, the summary judgment in the 1997 Action as to the termination claims. On October 30, 2001, Plaintiffs amended their complaint.

Plaintiffs bring their action on grounds that the judgment was a product of fraud on the Court because State Farm and Orrick "(a) fraudulently purport[ed] to represent a witness and fil[ed] fabricated comments and objections to a subpoena directed to that witness, without informing the witness or obtaining the witness' authorization[;] and (b) by fraudulently misrepresenting to [Plaintiffs] that the witness, a former State Farm official, had no documents or knowledge concerning the subject matter of the lawsuit." *Id.* at ¶ 2. The allegations of fraud stem around the conduct of Orrick, and thereby State Farm, in responding to certain subpoenas issued by Plaintiffs in the 1997 Action. *See* FAC at ¶¶ 31-35, 40-42. One such subpoena was issued against Henry Keller, a State

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3 The decision is currently on appeal with the Ninth Circuit; however, the Ninth Circuit has stayed its proceedings, on Plaintiffs' motion, pending resolution of the instant independent action. *See* Plaintiffs' Opposition to Defendants' Motion to Dismiss ("Opposition") at 2; *see also* Opposition, Exh. C.

Farm executive who had retired from his position in 1976.[4] *See Id.* at ¶¶ 31-15; *see also* Request for Judicial Notice ("RJN"), Exh. A. The other subpoenas were issued on State Farm itself. *See* FAC at ¶¶ 40-42.

With respect to the Keller subpoena, Plaintiffs allege that during the initial discovery period in the 1977 Action, Plaintiffs, through one of their counsel, Wallace Doolittle, subpoenaed Keller. *See* FAC at ¶¶ 18, 36. Keller contacted State Farm about the subpoena because he had "no familiarity with the litigation" and State Farm advised that it would handle the matter. *Id.* at ¶ 36; *see* FAC, Exh. E (Second Declaration of Henry Keller ("2d Keller Decl.")) at ¶ 11. Keller expected to receive information from State Farm about the litigation and expected some assistance with respect to the mechanics of responding to the subpoena, but did not hear from State Farm about it again. *See Id.*

In response to the Keller subpoena, Orrick filed objections, purportedly on Keller's behalf, to the location and

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4 With the subpoena, Plaintiffs sought the following:

1. Any and all documents regarding [State Farm], or any and all other State Farm entities from, and including, January 1, 1988 to the present.

2. Any and all correspondence with any representative, employee, officer, director, agent, consultant or and all other persons working for or with [State Farm], or any and all other State Farm entities from, and including, January 1, 1988 to the present.

RJN, Exh. A at Attachment A. Plaintiffs did not seek to depose Keller. *See Id.* at 1.

date of the production demanded and the relevance of the requests made. *See* FAC, Exh. B (Declaration of Wallace C. Doolittle re: Discovery Meet and Confer). In addition, Orrick objected on grounds that the requests (1) imposed an undue burden, (2) were unnecessarily broad, vague and ambiguous, (3) sought documents already in Plaintiffs' possession or obtainable from some other source, (4) sought disclosure of privileged material, and (5) violated Keller's privacy rights under the Florida Constitution. *See Id.* Thereafter, during a "meet and confer session" Orrick purportedly advised Plaintiffs that Keller "'ha[d] no documents and no knowledge concerning the subject matter of the lawsuit' and that it was therefore inappropriate for [Doolittle] to be unfairly burdening an elderly man such as [Keller]." *Id.* at ¶ 19. This conduct, according to Plaintiffs, constituted fraud sufficient to warrant an independent action to set aside the judgment because the objections and meet and confer were made without Keller's knowledge, absent his consent, and despite Keller's willingness to cooperate and produce materials[5] Plaintiffs contend would have led to the

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5 Plaintiffs specifically identify some of the material which would have been produced as, among other things, a letter prepared by Keller to State Farm in 1997 ("1997 Letter"), a video featuring Keller's presentation regarding independent contractor agents made in 1974 ("1974 Video"), and a video of Keller being interviewed by State Farm in 1988 ("1988 Video"). *See* FAC at ¶¶ 27-30. Plaintiffs purport that these materials pertain to the 1966 amendment of the agents' contracts to delete the terms "with or without cause" in the termination provision, and explicitly show that Keller rewrote the contract as an executive of State Farm in 1966 in response to the agents' concerns regarding State Farm's ability to arbitrarily terminate them. *See* Opposition at 5. This information, according to Plaintiffs, would have led Plaintiffs to Keller, who would then have

(continued...)

preparation of declarations by Keller stating that State Farm amended its agent contracts in 1966 to reflect its intent to change the termination provision from one which allowed State Farm to terminate at will to one which only allowed State Farm to terminate its agents for good cause. *See* Opposition at 5.

With respect to the State Farm subpoena, Plaintiffs allege that had Defendants properly produced all material responsive to the document request, Defendants would have produced the same documents Plaintiffs now contend would have led to Keller. *See* FAC at ¶¶ 40-42. Defendants' failure to produce the documents constituted, according to Plaintiffs, fraud on the Court warranting the independent action. Plaintiffs further assert that had the record in the 1997 Action contained the Keller Declarations, the it would have had evidence of the contemporaneous subjective intent of State Farm at the time of the 1966 revisions, and this Court would not have been able to find for Defendants. *See* FAC at ¶ 34. In support, Plaintiffs rely on a recent California court's finding that the same termination provision could be interpreted to be a "for cause" provision. *See Id.* at ¶ 21; *see also Id.*, Exh. C (*State Farm Mut.*

(...continued)
testified, that he rewrote the contracts with the intent of abandoning the at-will termination provisions. *See Id.; see also* FAC, Exhs. D (Declaration of Henry Keller ("Keller Decl.")) at ¶¶ 14-17 (stating that State Farm made efforts to amend the agent contracts to assuage the agents' concerns about being terminated arbitrarily, and State Farm made the changes so that the agents could no longer be terminated without cause) and E (2d Keller Decl.) at ¶¶ 4-5, 7, 10 (stating same).

Auto. Ins. Co. v. Wier, N. 82819, slip op. at 3 (Mendocino Superior Court July 3, 2001) ("Mendocino Order").[6]

Defendants now move to dismiss the action, arguing that the purported fraud claimed by Plaintiffs, even if true, is not a fraud upon the court, as it must be, to support an independent action. *See* Motion to Dismiss ("Motion") at 21. Specifically, Defendants contend that Orrick could not have committed fraud by virtue of having responded to a subpoena with valid objections on behalf of Keller, a long time State Farm employee. *See Id.* In addition, Defendants assert that the content of the material Plaintiffs contend were suppressed by Defendants during the 1997 Action was already before the Court and therefore would not have changed the outcome. *See Id.* Finally, Defendants argue that the failure to obtain the relevant evidence from Keller was entirely the product of Plaintiffs' own inadvertence and lack of due diligence.[7] *See Id.*

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6 Plaintiffs claim that the Mendocino Court expressly relied on the missing Keller declarations in making its determination. The Mendocino Order is not, however, as clear, stating only that it had before it "evidence which was not before [this Court] in the [1997 Action]" without identifying specifically to the documents it referred. *See* Exh. C at 3 (Mendocino Order).

7 Notably absent from Defendants' motion is any argument pertaining to the allegations in the FAC that State Farm failed to produce documents responsive to subpoenas, among which were the 1997 Letter and the 1988 Video. Because, however, the material alleged to have been withheld and the consequences thereof are the same as to both the State Farm subpoena and the Keller subpoena, the failure is immaterial.

LEGAL STANDARD

A Rule 12(b)(6) motion to dismiss tests the legal sufficiency of the claims asserted in the complaint. *Cahill v. Liberty Mutual Ins. Co.*, 80 F.3d 336, 337 (9th Cir. 1996). Dismissal of an action is appropriate only where it "appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Levine v. Diamanthuset, Inc.*, 950 F.2d 1478, 1482 (9th Cir. 1991). The Court will dismiss the complaint or any claim in it without leave to amend only if "it is absolutely clear that the deficiencies of the complaint could not be cured by amendment." *Noll v. Carlson*, 809 F.2d 1446, 1448 (9th Cir. 1987).

In determining a motion to dismiss, the Court must assume all factual allegations to be true and must construe them in the light most favorable to the non-moving party. *See North Star Int'l v. Arizona Corp. Comm'n*, 720 F.2d 578, 580 (9th Cir. 1983). However, the Court need not accept as true unreasonable inferences, unwarranted deductions of fact, or conclusory legal allegations cast in the form of factual allegations. *See Western Mining Council v. Watt*, 643 F.2d 618, 624 (9th Cir. 1981). Further, the Court need not accept as true allegations that contradict facts that have been judicially noticed or by exhibit attached to a complaint. *See Sprewell v. Golden State Warriors*, 266 F.3d 979, 988-89 (9th Cir. 2001).

ANALYSIS

Plaintiffs here seek to set aside the 2000 Order on the basis that Defendants intentionally and purposefully withheld certain information, the effects of which were to shield Keller and prevent Plaintiffs from obtaining declarations from him which stated that State Farm, in amending the termination provision in its agents contracts, intended to implement a "for

cause" termination policy. Defendants move to dismiss the action on grounds that the purported fraud claimed by Plaintiffs, even if true, is not a fraud upon the court, as it must be, to support an independent action because (1) Orrick did not commit fraud by having responded to a subpoena with valid objections on behalf of Keller, a long time State Farm employee; (2) the content of the material Plaintiffs seek were suppressed by Defendants during the 1997 Action was already before the Court and therefore would not have changed the outcome; and (3) the failure to obtain the relevant evidence from Keller was entirely the product of Plaintiffs' own inadvertence and lack of due diligence.

Federal Rule of Civil Procedure 60(b) provides, in part, that "any relief from a judgment shall be by motion as prescribed in these rules or by an independent action." An independent action is warranted "to set aside a judgment for fraud upon the court." Fed. R. Civ. Pro. 60(b).

Independent actions must, if Rule 60(b) is to be interpreted as a coherent whole, be "reserved for those cases of 'injustices which, in certain instances, are deemed sufficiently gross to demand a departure' from rigid adherence to the doctrine of res judicata." *United States v. Beggerly*, 524 U.S. 38, 46 (1998). To constitute fraud on the court, the alleged misconduct must "harm[] the integrity of the judicial process." *In re Levander*, 180 F.3d 1114, 1119-20 (9th Cir. 1999) (finding that "'[f]raud upon the court' should, we believe, embrace only that species of fraud which does or attempts to, defile the court itself, or is a fraud perpetrated by officers of the court so that the judiciary machinery can not perform in the usual manner its impartial task of adjudging cases that are presented for adjudication.") (internal citations omitted).[8]

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8 Defendants cite to a number of cases and for

(continued...)

Construing the allegations in Plaintiffs' favor, as this Court must, the fraud, simply, can be stated as Orrick having tricked Plaintiffs into believing that Keller had no responsive documents and no knowledge relevant to the litigation.[9] The

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(...continued)
the proposition that there are three factors which must be met before the fraud on the court might support an independent action under Rule 60(b). First, Defendants argue that the plaintiff must demonstrate that the defendant engaged in conduct that arises to the level of extrinsic fraud which, in other words, means that the conduct "so gravely subverted the judicial process as to deprive the plaintiff of his or her 'day in court.'" *See Green v. Ancora-Citronelle Corp.*, 577 F.2d 1380, 1384 (9th Cir. 1978). Second, Defendants argue that the plaintiff must demonstrate that the new evidence is material. *See Beggerly*, 524 U.S. at 47 n.4. Finally, according to Defendants, the plaintiff bears the burden of showing that he exercised due diligence in pursuing the evidence in the original action. *See MCI Tel. v. Matrix Comm.*, 171 F.R.D. 7, 9 (D. Mass. 1997). The Court does not agree with Defendants as to the rigid formula they present in determining whether the independent action is justified. However, the Court notes that the factors and analysis identified by Defendants are consistent with the test set forth above by this Court.

9 Here, Plaintiffs alleged that Defendants intentionally withheld evidence which would have otherwise led Plaintiffs to Keller by "pretending" to represent Keller, filing false objections on his behalf absent his knowledge or consent, and representing to Doolittle that Keller did not have any documents responsive to the subpoena and did not have any knowledge as to the litigation. Defendants argue that Orrick did not "pretend" to represent Keller and instead did

(continued...)

Court must, therefore, determine whether Defendants' efforts to convince Plaintiffs that Keller had nothing responsive constituted a fraud upon this Court which would justify the relief sought.

Helpful in the analysis is a discussion of two cases in which the Second Circuit and Ninth Circuit respectively considered the issue of whether non-disclosure or perjury constituted fraud on the court. The Second Circuit, in *Gleason v. Jandrucko*, 860 F.2d 556 (2nd Cir. 1988), found that non-disclosure of evidence or perjury, without more, does not constitute fraud on the court where the allegedly defrauded party had the opportunity to challenge the alleged perjured testimony or non-disclosure. *See Id.* at 559-60. In *Gleason*, the plaintiff sought to set aside the judgment against him in light of having discovered that the police officers who testified against him lied about the strength of the eye witness accounts. *See Id.* at 558. The Second Circuit affirmed the lower court's finding that the alleged perjury could not sustain an independent action because (1) the plaintiff could have deposed the eyewitnesses

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represent him in light of the fact that Keller, by his own declaration, claims to have contacted State Farm about the subpoena and was told that it would take care of it. In addition, Defendants argue that the objections to the subpoena were not "false" as contended by Plaintiffs but instead valid. The Court is disinclined to construe Orrick's conduct with respect to the representation of Keller was anything but proper especially in light of Keller's declaration that he called State Farm about the subpoena and was told that State Farm would take care of it. In addition, at first glance, the objection made on Keller's behalf are innocuous. The Court, however, makes no conclusive finding to the extent that doing so is not necessary to the resolution of the motion here.

and introduced evidence at trial to impeach the police officers' testimony; and (2) the issue of the officers' credibility was before the court. *See Id.* at 559-60. The Second Circuit concluded that the plaintiff could not, after the fact, claim fraud on the court based only on alleged perjury by the officers, which he could and should have challenged during the trial. *See Id.*

In *Levander*, 180 F.3d 1114 (9th Cir. 1999), the Ninth Circuit found that *Gleason* did not apply where the allegedly defrauded party had no opportunity to challenge the allegedly perjured testimony or non-disclosure of evidence. *See Id.* at 1119-20. In *Levander*, the plaintiff brought an independent action to set aside judgment for attorney's fees on grounds that the party against whom attorney's fees were imposed, the Corporation, had defrauded both the plaintiff and the court by having testified under oath that it had not transferred any of its assets when in fact it had transferred its assets to nineteen corporate entities, which then conveyed the assets to a partnership, which then sold the assets to a former employee for one dollar. *See Id.* at 1117, 1120. Relying on the Corporation's alleged perjured statements, however, the court imposed attorneys' fees on the Corporation rather than the partnership, the party with the assets. *See Id.* Because neither the court nor the plaintiffs knew that the partnership existed and, as a result, the issue was never before the court, the Ninth Circuit affirmed the lower court's finding that the perjury constituted a fraud upon the court which would sustain the independent action to set aside the judgment. *See Id.*

Construing the facts alleged to be true, Orrick, like the defendants in *Levander* who testified under oath that it still maintained all of the assets, affirmatively put Plaintiffs on the wrong track by representing to Plaintiffs Keller's position and assuring Doolittle that Keller had no documents and no knowledge of relevant facts. Orrick's conduct, however, falls short of the defendants' efforts described in *Levander* in that Orrick did not have State Farm testify under oath that Keller

had no information. In addition, it did not make concerted efforts to conceal or disguise the circumstances surrounding the 1966 amendment of the termination provision. *See generally England v. Doyle*, 281 F.2d 304, 310 (9th Cir. 1960) (finding that the plaintiff's non-disclosure of a stipulation, among other things, did not display an "unconscionable plan or scheme" designed to influence the decision of the court to warrant setting aside the judgment with an independent action). Instead, Orrick objected to subpoenas on behalf of Keller and represented to Plaintiffs that Keller had no responsive documents or information. All the while, Plaintiffs knew enough to have subpoenaed Keller personally, as opposed to having had subpoenaed the person most knowledgeable at State Farm.

That Doolittle, on behalf of Plaintiffs, made a tactical decision not to pursue production from Keller by seeking to compel discovery based upon Orrick's objections or representation is more analogous to the plaintiff's failure to test the police officers' testimony in *Gleason* where the identity of the eyewitnesses was known to the plaintiff and the issue of the officers' credibility was before the court. Mindful that the relief sought by Plaintiffs here under Rule 60(b) is appropriate in limited circumstances and reserved for those cases of injustice which "are deemed sufficiently gross to demand a departure from rigid adherence to the doctrine of res judicata," *Beggerly*, 524 U.S. at 46, the Court finds that the relief cannot be invoked where, as here, a party makes a tactical decision which, in the end, results in the non-disclosure of evidence it later finds is important to its case. Therefore, the Court GRANTS Defendants' motion to dismiss. The dismissal is with prejudice in light of the Court's finding that Plaintiffs are unable to cure the deficiencies identified here.

CONCLUSION

For the foregoing reasons, the Court GRANTS Defendants' motion to dismiss. The action is DISMISSED WITH PREJUDICE.

IT IS SO ORDERED.

Dated: January 31, 2002

_____/s/_____
MARTIN J. JENKINS
U.S. DISTRICT JUDGE

APPENDIX F

UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

WILLIAM A. APPLING, et al., Plaintiffs,	)	No. C 01-3181 MJJ
v.	)	**JUDGMENT IN A CIVIL CASE**
STATE FARM MUTUAL AUTO. INS. CO., et al Defendant.	)	

__ **Jury Verdict.** This action came before the Court for a trial by jury. The issues have been tried and the jury has rendered its verdict.

X **Decision by Court.** This action came to trial or hearing before the Court. The issues have been tried or heard and a decision has been rendered.

IT IS ORDERED AND ADJUDGED
that the Court GRANTS Defendants' motion to dismiss.

February 6, 2000
Date

Richard Wieking
Clerk

/s/
(By) Deputy Clerk

(3)

No. 04-54

In The
Supreme Court of the United States

WILLIAM A. APPLING, et al.,

Petitioners,

v.

STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY, et al.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONDENTS' BRIEF IN OPPOSITION

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August 18, 2004

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QUESTIONS PRESENTED

Petitioners are former State Farm agents whose contracts were terminated by State Farm Mutual Automobile Insurance Company, State Farm Fire and Casualty Company, State Farm Life Insurance Company, and State Farm General Insurance Company (collectively "State Farm"). The contracts provided that either party could terminate the contract simply by giving written notice. State and federal courts throughout the country have held repeatedly that this termination language in the State Farm contract unambiguously permitted the contract to be terminated at the will of either party. Despite these cases, Petitioners filed suit claiming that State Farm's termination of their contract was wrongful. Petitioners argued that, as a matter of offensive collateral estoppel, a prior unpublished memorandum decision by the Ninth Circuit trumped all of the prior contrary decisions and established, as a matter of law, that State Farm's agreement could be terminated only for good cause.

Applying the principles established by this Court in *Park Lane Hosiery Co. v. Shore,* 439 U.S. 322 (1979), the district court determined that, in its exercise of discretion, offensive collateral estoppel was not appropriate. Among other things, the district court observed that the plethora of prior authority finding the same contract language to be terminable at will made it inappropriate to give preclusive effect to contrary language in the unpublished decision. The Ninth Circuit held that the district court had properly exercised its discretion in reaching this conclusion. On the merits of the contract construction issue, the Ninth Circuit also affirmed the district court's determination that, as a matter of law, the contract was terminable at will.

QUESTIONS PRESENTED – Continued

Dissatisfied with the district court's ruling, Petitioners waited more than a year after judgment was entered and then filed an independent action alleging that the summary judgment should be set aside because State Farm and its counsel had allegedly failed to produce in discovery certain documents in the possession of a retired State Farm executive. The district court, which was fully familiar with the prior summary judgment proceedings, determined that Petitioners' allegations did not meet the stringent standards required to set aside a prior judgment. The Ninth Circuit concluded that the district court had acted well within its discretion and affirmed that judgment as well.

Properly framed, the Petition raises the following issues:

1. Did the Court of Appeals for the Ninth Circuit err in determining that the district court acted within its discretion in refusing to give preclusive offensive collateral estoppel effect to dicta in a prior unpublished memorandum decision which was contrary to every other published and unpublished decision issued by state and federal appellate courts across the country construing that same contract?

2. Did the same Court of Appeals for the Ninth Circuit err in affirming the district court's exercise of discretion in concluding that Petitioners' allegations that documents had not been produced in discovery in response to an overbroad third party subpoena did not amount to fraud on the court and did not warrant setting aside the prior summary judgment?

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

Respondent State Farm Mutual Automobile Insurance Company is a mutual insurance company owned by its policyholders. Respondents State Farm Fire and Casualty Company, State Farm Life Insurance Company and State Farm General Insurance Company are wholly-owned subsidiaries of Respondent State Farm Mutual Automobile Insurance Company.

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STATEMENT OF THE CASE

In April 1997, Petitioners filed suit against State Farm contending, among other things, that State Farm acted improperly in terminating the contracts of more than twenty of the named Petitioners. The contracts permitted either party to terminate the contract simply by giving written notice. Petitioners contended that the contract language permitting termination on written notice was ambiguous and allowed termination only on a showing of good cause. Petitioners' wrongful termination claims arose under state law in several different states, including California.

Petitioners and State Farm filed cross-motions for summary judgment on Petitioners' wrongful termination claims. State Farm sought summary judgment on the ground that, as a matter of law, the contract was unambiguously terminable at will. Petitioners sought summary judgment on the ground that language in an unpublished Ninth Circuit memorandum decision was collateral estoppel on the issue of whether the contract was terminable only for good cause. That prior memorandum decision affirmed summary judgment in favor of State Farm on a former agent's wrongful termination claim but indicated, in dicta, that the contract was susceptible of a good cause construction. *Sandberg v. State Farm Mut. Auto Ins. Co.*, 182 F.3d 929 (9th Cir. 1999) (mem disposition), *cert. denied*, 528 U.S. 1118 (2000).

Recognizing that the decision whether to give offensive collateral estoppel effect to a prior decision rests within its discretion, the district court concluded that the prior *Sandberg* decision should not be given collateral estoppel effect. Pet. Supp. App. at 3a-4a. The district court noted that several other published and unpublished

appellate decisions had repeatedly held that the State Farm contract was terminable at will. Pet. Supp. App. at 7a. The district court further noted that the *Sandberg* decision had actually affirmed the decision by State Farm to terminate the contract. As such, the language in *Sandberg* dealing with construction of the contract was not necessary to the judgment. *Id.* at 9a.

The Ninth Circuit affirmed the district court's decision. The Ninth Circuit recognized that the decision whether to apply collateral estoppel rested within the district court's discretion. Pet. App. at 11a. The Ninth Circuit held that the district court properly applied the standards established in *Park Lane Hosiery* and acted within its discretion in determining that no offensive collateral estoppel effect should be given. The Ninth Circuit agreed that the "stark landscape of inconsistent prior interpretations of the termination clause weighs heavily in favor of granting *Sandberg* no preclusive effect." Pet. App. at 13a. The Ninth Circuit cited to nine published and unpublished decisions wherein federal and state courts had construed the State Farm contract to be terminable at will, under the relevant state's law. Pet. App. at 14a.

After the district court's summary judgment decision, Petitioners filed an independent action to set aside the summary judgment on the ground that State Farm and its counsel had withheld documents from discovery directed at a third party witness. The discovery consisted of a 1998 subpoena directed at a former State Farm executive who retired in 1976. That subpoena sought documents possessed by the former executive generated after January 1, 1988 – twelve years after the executive left State Farm. State Farm, through its counsel, interposed objections to the subpoena on behalf of the former executive. Thereafter,

Petitioners took no further action. They made no attempt to depose the former executive or to follow up on the subpoena.

Accepting Petitioners' allegations at face value, the district court nonetheless concluded that State Farm and its counsel did not commit a fraud on the court in responding to the subpoena. The district court noted that State Farm's objections to that subpoena were innocuous, and the witness in question had authorized State Farm to respond to the subpoena on his behalf. Pet. Supp. App. at 32a n.9. The district court concluded that Petitioners' allegations did not provide a basis to set aside the prior judgment and exercised its discretion to dismiss the complaint. The Ninth Circuit affirmed the district court's decision, concluding that the district court, which had issued summary judgment in the first instance, was well within its discretion in determining that it had not been victimized by a fraud on the court.

ARGUMENT

I

PETITIONERS HAVE NOT ARTICULATED A REASON JUSTIFYING DISCRETIONARY REVIEW BY THIS COURT

Petitioners' arguments in their petition amount to nothing more than a restatement of their belief that the Ninth Circuit's dissenting opinion was correct and the majority opinion was incorrect. Petitioners do not contend that the Ninth Circuit's decision conflicts with any decision of another circuit or with any decision of any state court of last resort. Nor have Petitioners contended that the Ninth Circuit decision involves a gross departure from the accepted

and usual course of judicial proceedings or that the Ninth Circuit's decision presents an important question of federal law or somehow conflicts with any prior decision of this Court.

The true gist of each of Petitioners' questions is whether, in a highly fact-specific context, the district court properly exercised its discretion. With respect to the district court's refusal to apply offensive collateral estoppel effect to language in a prior, unpublished Ninth Circuit decision, the district court considered each of the factors identified in this Court's prior decision in *Park Lane Hosiery* and concluded, on balance, that it was not appropriate to give preclusive effect to language in that memorandum decision. Petitioners do not contend that *Park Lane Hosiery* does not give broad discretion to district courts to make this type of determination.

Similarly, to the extent that the Petition challenges the dismissal of their independent action, Petitioners are essentially challenging the district court's exercise of discretion based on highly case-specific facts. It is well established that the decision to set aside a prior judgment based upon alleged fraud on the court rests soundly within the discretion of the district court. *Levi Strauss & Co. v. Shilon*, 121 F.3d 1309, 1313 (9th Cir. 1997). Petitioners do not take issue with this settled rule of law. Rather, Petitioners' challenge amounts to nothing more than a complaint about the manner in which the district court, which was the same court that previously granted summary judgment, weighed the relevant factors in exercising its discretion.

Neither of the issues presented by Petitioners raise any issue of general application or a conflict with any decision previously issued by this Court, by any other

circuit court or by any state court of last resort. There is no basis or need for the Petition to be granted.

II

THE LOWER COURTS DID NOT ERR IN RULING IN FAVOR OF STATE FARM

In both the main action and in Petitioners' independent action, Petitioners' claims were properly resolved in favor of State Farm. When the Ninth Circuit affirmed the summary judgment in favor of State Farm, each and every published decision construing State Farm's contract had concluded that the contract was terminable at will. This included a recent *en banc* decision by the Eighth Circuit. *Olander v. State Farm Mut. Auto Ins. Co.*, 317 F.3d 807 (8th Cir. 2003) (*en banc*), *cert. denied*, 124 S. Ct. 179 (2003). Several unpublished decisions had reached the same conclusion including three unpublished decisions issued by California courts. In asking the district court to impose offensive collateral estoppel by reason of the Ninth Circuit's prior unpublished memorandum decision in *Sandberg*, Petitioners were essentially arguing that certain language in the *Sandberg* decision trumped these many other state and federal cases that had reached the contrary conclusion. Faced with overwhelming authority to the contrary, the district court acted well within its discretion to conclude that, under the principles announced by this Court in *Park Lane Hosiery*, it would be inappropriate to give collateral estoppel effect to the *Sandberg* memorandum decision.

The district court's decision not to give preclusive effect to language in the unpublished *Sandberg* decision was further supported by the peculiar circumstance surrounding

that decision. The Ninth Circuit in *Sandberg* actually affirmed summary judgment in favor of State Farm as to the former agents' claim for wrongful termination. The *Sandberg* court determined that the undisputed facts established that State Farm had good cause to terminate the contract. It was in this context that the unpublished memorandum decision in *Sandberg* stated that the contract was reasonably susceptible of either an at will or good cause construction. While the Ninth Circuit declined to characterize the language in *Sandberg* as dicta, the at will/good cause determination made in *Sandberg* was superfluous to the *Sandberg* holding. At the very least, the fact that this portion of the opinion was not the basis of the summary judgment provided additional reason for the district court and Ninth Circuit's determination that it should not be given preclusive effect.

Petitioners' argument that the majority opinion failed to give *stare decisis* effect to the *Sandberg* dicta rests on several faulty assumptions. First, as an unpublished decision, the *Sandberg* decision was never intended to be *stare decisis*. Second, as to State Farm, the unpublished *Sandberg* decision could be binding vis-a-vis third parties only under principles of **offensive** collateral estoppel which the lower courts found were not met. Third, the majority opinion concluded that the *Sandberg* dicta did not correctly apply California law to State Farm's contract language. Under these circumstances, it can hardly be said that the Ninth Circuit's majority opinion improperly decided the contract construction issue on the merits.

Similarly, the lower courts' determination that the prior summary judgment should not be set aside based on Petitioners' "fraud on the court" claim is well supported by the record. It is especially significant that the district court which was asked to make the decision was the same

court that had issued summary judgment in the first place. If and to the extent that any allegations of discovery abuse were truly material to its decision, the district court was uniquely situated to make that call. Under these circumstances, the district court properly exercised its discretion to conclude that mere allegations that documents were not produced in discovery in response to a patently deficient subpoena did not amount to fraud on the court.

Petitioners seriously mischaracterize their own allegations of supposed misconduct. Petitioners assert that State Farm fraudulently purported to represent a third party witness. In fact, based upon declarations included as part of Petitioners' complaint, the district court concluded that it was "disinclined to construe Orrick's conduct with respect to the representation of Keller [the third party witness] [as] anything but proper especially in light of Keller's declaration that he called State Farm about the subpoena and was told that State Farm would take care of it." Pet. Supp. App. at 32a n.9. Moreover, while the court concluded that the validity of the objections made to the subpoena on Keller's behalf were not necessary to the resolution of the motion to dismiss, the court described those objections as "innocuous." *Id.* Petitioners made no allegation that they ever took any steps to further pursue their request for documents. Nor did they make any allegations that they had ever contacted Keller themselves or proposed any other witnesses concerning the matters supposedly known to Keller. Essentially, as the district court found, plaintiffs made a tactical decision not to pursue production from Keller which simply resulted in non-disclosure of evidence which it later alleged to be important to their case. Pet. Supp. App. at 34a.

While Petitioners try to contend that the lower courts' decisions to dismiss their independent action were based

solely upon Petitioners' own lack of due diligence, an analysis of both the district court and Ninth Circuit's decisions demonstrate that Petitioners' lack of diligence was only one factor considered by the lower court. Equally important was the fact that the alleged non-disclosure of documents in the discovery process did not constitute a fraud on the court and the determination that the supposed conduct did not meet the high standard established by this Court in *United States v. Beggerly*, 524 U.S. 38, 47 (1998) which requires a "grave miscarriage of justice" to set aside a prior judgment.

CONCLUSION

For the reasons set forth above, Respondents respectfully request that the Petition for a Writ of Certiorari be denied.

Respectfully submitted,

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